BANK OF PAPUA NEW GUINEA

ANNUAL REPORT AND FINANCIAL STATEMENTS

31 DECEMBER 2020

BANK OF PAPUA NEW GUINEA

ANNUAL REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDING 31 DECEMBER 2020

For the advantage of the people of Papua New Guinea, the objectives of the Central Bank are:

(a) to formulate and implement monetary policy with a view to achieving and maintaining price stability; and

(b) to formulate financial regulation and prudential standards to ensure stability of the financial system in Papua New Guinea; and

(c) to promote an efficient national and international payments system; and

(d) subject to the above, to promote macro-economic growth in Papua New Guinea.

Central Banking Act 2000

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Governor's Foreword


Mr Loi M. Bakani CMG, Governor and Chairman of the Board

2020 was a year of unprecedented economic downturn brought on by a global health crisis. The COVID-19 pandemic had a devastating impact on the world's population and economies, with governments imposing lockdowns and other containment measures to protect their people. The pandemic and containment measures resulted in the largest contraction in the global economy since the Great Depression in the 1930s. Governments implemented a wide range of policy measures, packages and unconventional policies to combat the pandemic and stimulate their economies.

In Papua New Guinea (PNG) the effects of the pandemic included a decline in economic activity during the year. Like many other countries, the PNG Government introduced various measures to contain the pandemic, including a nation-wide State of Emergency and lockdowns, as well as travel restrictions. The pandemic and containment measures led to a decline in economic activity of 3.8 percent, the first decline after eighteen consecutive years of growth, as companies scaled down their operations and laid off workers to adhere to the COVID-19 protocols. This had an adverse impact on the Government's revenue collections and exerted pressure on budget financing. The fall in international commodity prices for most of PNG's exports resulted in lower export receipts relative to import demand, which produced a deficit in the balance of payments. The sectors most affected were transportation, accommodation and food services and other services. The closure of the Porgera Gold Mine from April 2020, due to the expiry and non-renewal of its Special Mining Lease, also contributed to the decline.

The economy started to recover in the second half of the year as the Government introduced a fiscal stimulus package and various measures to boost economic activity.

To support the Government's efforts and assist economic activity, the Bank of Papua New Guinea ("the Bank" or "BPNG") implemented several policy measures. These included easing its monetary policy stance by reducing its policy rate, the Kina Facility Rate, from 5.00 percent to 3.00 percent. Additional liquidity of around K1.4 billion was injected into the banking system with the reduction in the Cash Reserve Requirement (CRR) from 10.0 percent to 7.00 percent and implementing a quantitative easing program through early redemption of Government securities from their holders. The Bank relaxed some of its prudential reporting requirements. The Bank also supported the measures introduced by the commercial banks, to assist their clients through the deferment of loan interest payments, as well as reduction in interest rates and fees for some of their products.

The pandemic and containment measures disrupted domestic supply chains and increased demand for health services and various seasonal products. These factors contributed to the high inflation recorded in 2020, with the annual headline inflation peaking at 6.3 percent in the June quarter, before declining to 5.1 percent in the December quarter, as the containment measures were slowly eased. With the declining inflation, the Bank maintained its accommodative stance throughout 2020 after the easing in April to support economic activity.

PNG entered into an eighteen month International Monetary Fund (IMF) Staff Monitored Program (SMP) in February 2020. The SMP aimed to assist the Government implement sound economic and social policies to ensure macroeconomic stability. BPNG met the three quantitative targets and three structural benchmarks set.

The year 2020 marked the end of the 5 year period of the Bank's 2016-2020 Strategic Plan. Achieving the final stages of the Plan was made difficult as most of the Bank's operations and activities were affected, mainly by the COVID-19 pandemic.

The Bank's Business Continuity Plan was invoked several times during the year, initially to deal with a major workplace air conditioning problem, followed almost immediately by the pandemic. The Bank scaled down operations, rostered staff responsible for critical functions to attend the workplace in shifts and enabled other staff to work from home or from offsite locations. While the Bank was able to conduct critical operations throughout the year, many of the other tasks and projects planned for 2020 were put on hold. For example, many of the planned projects were unable to proceed as travel restrictions prevented onsite support from key advisors.

The Bank's risk management strategies and processes were put to real-life tests as the COVID-19 situation highlighted operational risks, key person risks and cyber security risks, particularly as some staff contracted the virus in spite of the protection protocols put in place. Overall, the Bank's risk management met the challenges and enabled the Bank to deliver its critical services throughout the year.

> “The Government introduced a fiscal stimulus package and various measures to support economic activity.”

Turning to the impact of the pandemic on the broader economy and foreign exchange (FX), even though COVID-19 slowed economic activity, the mineral sector continued to perform well with good foreign exchange inflows into the domestic market. The external financing for the National Budget assisted with the international reserves, as did financing from the IMF Rapid Credit Facility in response to the COVID-19 pandemic.

The Bank used interventions to help meet demand in the FX market. To ensure sufficient liquidity in the FX spot market, the Bank issued a Foreign Exchange Market Directive in July 2020 to suspend trading of forward exchange contracts by the Authorised Foreign Exchange Dealers.

Although the Bank's plans for an upgrade to the KATS system were delayed due to the pandemic, other developments to enhance the National Payments System continued. Work continued on the REPS program to link existing services and improve access to digital payments, including the Instant Payment Transactions (IPT) facility, which provides real time retail payments among REPS member institutions.

Governor's Foreword

As the Banker to the Government, BPNG held discussions and coordinated activities with the Department of Finance during 2020 to continue improvement to banking services provided to the Government and ensure compliance with requirements such as anti-money laundering legislation.

All Government transactions through the Electronic File Transfer function have now been extended to cover all cash related payments, including provincial and district development and recurrent grants, statutory body transfers and grants to other Government institutions. This electronic payment system is faster and easier to implement and prevents fraudulent transactions.

To manage cash flow through the additional challenges presented by the pandemic, the Government amended the *Central Banking Act 2000* in September 2020 to increase the flexibility of the Temporary Advance Facility (TAF). The new TAF limit was set as 12 percent of the average revenue and grants of the preceding 2 years and the term of the facility was extended from 6 months to 12 months.

The National Financial Inclusion Strategy 2016-2020 was successfully concluded at the end of 2020. Through the Centre of Excellence for Financial Inclusion (CEFI), the Bank played a pivotal role in promoting and facilitating financial inclusion activities during 2020. Financial awareness activities included information sessions, mini-shows and expositions, updating financial inclusion stakeholders on technology and digital financial services innovation.

Financial Analysis and Supervision Unit (FASU) continued to play an important role in providing surveillance on money laundering and terrorism financing. Its activities were affected by the pandemic, with the focus more on offsite assessments. FASU signed three memoranda of understanding in 2020 to strengthen information sharing with domestic agencies.

With the pandemic restricting the Bank's undertakings to critical functions, most training and development activities throughout the year were scaled back and held online. The Bank continued to receive online assistance and support from the IMF, the Reserve Bank of Australia, the Reserve Bank of New Zealand, the World Bank and its affiliate IFC, the Asian Development Bank, the Pacific Financial Technical Assistance Centre (PFTAC), South East Asian Central Banks Training Centre (SEACEN) and the South Pacific Centre of Central Banking (SPCCB) at Griffith University, Australia.

I extend my sincere thanks to my fellow Board members, the Deputy Governor, Assistant Governors, the senior management and staff of the Bank for their commitment and support during a very difficult and challenging year. In particular, I acknowledge the support and valuable contribution the Late Simon Tosali OBE made to the Bank as a Board member.

As this report shows, 2020 was an extremely challenging year, in which the Bank's contingency plans for operating in unprecedented circumstances were faced with a series of hard tests. We were forced to embrace new ways of doing things, to learn new skills, to acquire knowledge to handle the unknown and to cope with personal risk. I am very proud to be able to present the 2020 Annual Report, which demonstrates how well the Bank of Papua New Guinea and its staff perform our core functions even in the toughest circumstances to the benefit of the people of Papua New Guinea.

Loi M. Bakani CMG

Governor and Chairman of the Board and Registrar of Savings and Loan Societies

Highlights

The Hon. Bart Philemon, former Board member of BPNG and a former Member of Parliament for Lae, joined Governor Loi M. Bakani CMG and Assistant Governor Elizabeth Genia (front row), with staff members of the Bank in Lae and representatives of the construction contractor and project manager to celebrate the official opening of the Bank's new staff accommodation in Lae.

The Bank expands footprint in Lae

The Bank of Papua New Guinea's physical presence in Lae, Morobe Province increased during 2020, with the official opening of modern apartment-style accommodation for Bank staff.

L-R: Governor Loi M. Bakani CMG congratulates Mr Israel Anduari (Building Manager, Lae CPF) on the successful completion of the staff accommodation, with Assistant Governor Mrs Elizabeth Genia.

Board meetings

The Bank's Board meets four times each year. Usually 2 of those 4 meetings are held outside Port Moresby, to give Board members the opportunity to see firsthand how the Bank's policies and activities relate to the broader PNG community. However, travel restrictions due to COVID-19 during 2020 meant 3 meetings were held in or close to Port Moresby, including the delayed June quarter Board meeting that was held in July.

***Front** L-R: Mr John Paska (Board Member), Governor Loi M. Bakani CMG (Chairman), Bishop Denny Guka (Board Member), Assistant Governor Elizabeth Genia, Mr John Leahy (Board Member).* ***Back** L-R: Mr Richard Kuna (Board Member), Assistant Governor Simon Gaius, Deputy Governor Joseph Teria (Board Member), Assistant Governor Ellison Pidik, Mr David Toua (Board Member).*

Highlights

Financial awareness continues to spread across PNG

The Bank hosted a Financial Inclusion mini-Expo in Kavieng, New Ireland Province in 2020.

L-R: Mr John Paska (Board Member), Mr George Awap (Department Manager, Financial Systems Development, BPNG), Mr Dominic Sikakau (Program Manager, SME Accelerator Program), Governor Loi M. Bakani CMG, Mr Augustine Birie (AB Consulting), Mr Benny Popoitai MBE (Director, Financial Analysis & Supervision Unit).

Local dancers perform a Malangan ceremonial dance, highlighting the rich culture of New Ireland, during the Bank's Financial Inclusion Mini-Expo in Kavieng.

Building awareness in rural areas

Regional shows and cultural events have long been ideal venues for the Bank to provide information about money matters for people in rural and remote areas. In December 2020 Bank staff set up an information stand at the very popular East Sepik Culture and Agriculture Show, a great opportunity to update the local people on financial services developments.

Tradition meets technology

Traditionally attired participants at the Show, showing interest in the Bank's information brochures about electronic payments, demonstrate that the timelessness of traditional culture can go hand-in-hand with time-saving modern technology.

Safe and fair workplace

The Bank's commitment to being a safe and fair workplace strengthened during 2020. While implementation of gender equity and social inclusion (GESI) principles and practices continued, the Bank also raised awareness about Family and Sexual Violence (FSV) with education sessions for staff. The focus of the sessions was on safety, victim support and prevention of incidents.

The Bank's GESI Focal Points (GESI leaders within the Bank) attended a train-the-trainers workshop dealing with family and sexual violence, conducted by the Business Coalition for Women (BCFW), in preparation for the introduction of a FSV Policy in the Bank.

***Front** L-R: Brenda Koan, Raylene Semi, Sallyanne Romel, Aiva Aku, Assistant Governor Elizabeth Genia, Rosemary Lalaga, Maryanne Kani, Frieda Kamakom, Tommy Minjura.*

***Back** L-R: Justin Wohuinangu, Angesula Jogamup, Naomi Kedea, John Nema, George Geberi, Zebedee Arope, Harry Paul.*

Bank staff say NO to violence against women

The FSV awareness session was strongly supported within the Lae CPF, with staff clearly demonstrating their support for BPNG's position against family and sexual violence.

***Front** L-R: Benek Beriso, Paula Kaidong, Jack Dalele.*

***Back** L-R: Veronica Bonasu, Aloma Kaniniba, Agulea Poigeno, Margaret Bagu, Damarish Tiling, Agnes Kose, Jason Boude, Frieda Kamakom.*

The entire staff of BPNG in Lae gathered together to show their commitment to stopping violence against women.

Mission Vision Values

Mission

The Bank of Papua New Guinea's MISSION is to serve the people of Papua New Guinea by conducting effective monetary policy and maintaining a sound financial system. We will act at all times to promote macro-economic stability, provide a first class payments system, issue the national currency and help foster economic growth of our country.

Vision

A contemporary central bank and regulator excelling in performing our core functions and making a distinct and valuable contribution to the economic well-being of Papua New Guinea.

Values

With **INTEGRITY** we build good governance and credibility.

With **EFFICIENCY** we produce quality results, on time and on budget.

With **TRANSPARENCY** our decisions stand scrutiny.

Through **ACCOUNTABILITY** we take responsibility for our decisions and actions.

Through **TEAMWORK** we benefit from sharing skills, knowledge and experience.

Through **PROFESSIONALISM** we strive for best practice.

Governance

Governor and Chairman
Loi M. Bakani CMG

Deputy **Governor** Joseph Teria

Mr John Leahy

Mr John Paska

Mr Richard Kuna

Bishop Denny Bray Guka

Mr David Toua

Late Mr Simon Tosali OBE

Members of the Board of the Bank of Papua New Guinea in 2020

The Bank of Papua New Guinea has adopted best corporate governance principles, practices and standards. In line with the CBA 2000, its strategic plans and code of conduct, the Bank's adherence to good corporate governance is reflected in its operations, processes, procedures and systems.

These practices are embedded in the role, structure and composition of the Board, including its committees, and in the Bank's organisational structure and management roles, management reporting systems and effective internal and external audit processes.

Under the CBA 2000, the Governor and the Board of the Bank have distinct roles and responsibilities. The Governor is directly responsible for the formulation of monetary policy and regulation of the financial system. The Board's role is to determine the policy of the Bank in all other aspects of its functions.

The Governor determines all matters of internal management, while the Board adopts appropriate practices of good governance to assist and oversee the Governor in performing his roles and responsibilities.

Composition of the Board

Under the terms of the CBA 2000, the Board comprises members who are either *ex officio* (by virtue of the offices they hold) or *non-ex officio* (appointed by the Head of State acting on advice from the NEC).

The Governor, who is also Chairman of the Board, is appointed by the Head of State acting on advice, for a term of up to seven years. Selection and appointment of the Governor is a stringent process, as required by the terms of the *CBA 2000* and the *Regulatory Statutory Authorities (Appointment to Certain Offices) Act 2004*. The Act specifies that the Governor is "of good moral standing" with recognised professional experience in banking and financial matters.

The Deputy Governor, appointed by the Governor in consultation with the Minister for Treasury for a term of up to 5 years, is a member of the Board and chairs the Board in the absence of the Governor. The Governor has the discretion to appoint either one or two Deputy Governors.

The other members of the Board include five *ex officio* members from a range of prominent institutions within the PNG community (church, regulatory, workers' representation and industry bodies) and up to three *non-ex officio* members.

All Board members are required by statute to meet the key standards of good governance.

The position of the Chairman of the Securities Commission was vacant in 2020.

Management Structure

The Bank has established a management structure with clear reporting lines, conforming with the principles of good governance. (See Organisation Chart page 40.)

Each Assistant Governor is responsible for a functional group comprising related departments. A number of inter-departmental management committees are established to perform various functional and management responsibilities for and on behalf of the Governor.

In line with this structure, during 2020 the Deputy Governor, the Assistant Governors, the Internal Audit Department Manager, Director FASU and the Corporate Secretary reported directly to the Governor. Other Department Managers reported either to the Deputy Governor or to an Assistant Governor.

Funding

The Bank's independence, including financial independence from the Government, is essential to maintaining the integrity of its operation and policy decision-making. Under the CBA 2000, the Bank is a self-funding institution, with its own capital and reserves.

The Board

Governor and Chairman

Loi M. Bakani CMG

Mr Loi M. Bakani CMG was appointed Governor and Chairman of the Board in December 2009. In December 2016 he was reappointed for an additional 7 years term.

He is also the Registrar of Savings and Loan Societies in PNG.

Mr Bakani is also a Member of the Board of South East Asian Central Banks (SEACEN), the Alternative Governor for PNG on the IMF Board of Governors, Chairman of the Centre for Excellence in Financial Inclusion (CEFI), Director of the PNG Institute of Directors (PNGID), Director of the PNG Institute of Banking & Business Management (IBBM) and a Member of the Advisory Board of Port Moresby Senior AFL competition.

He holds a Bachelor of Economics from the University of Papua New Guinea and a Master's degree in Commerce majoring in Economics from the University of Wollongong, Australia.

Deputy Governors

Mr Joseph Teria

Mr Teria was appointed Deputy Governor and an *ex officio* member of the Board on 1 February 2019.

A career central banker of more than 40 years' experience, Mr Teria commenced employment with the Bank of Papua New Guinea in 1979. After holding a number of senior management positions in the Bank, in the areas of foreign reserves management, foreign exchange control and management, financial accounting and administration, Mr Teria was appointed the Assistant Governor responsible for Finance & Payments in October 2011.

He holds a Master's degree in Commerce from the University of Sydney, Australia.

Members of the Board

Mr John Leahy

Mr Leahy was appointed *ex officio* member of the Board in March 2008, in his capacity as President of the Papua New Guinea Chamber of Commerce and Industry.

Mr Leahy is in private practice as a lawyer in PNG. He is also a Director of a number of companies, including the BNG Trading Group Ltd and its subsidiaries.

He holds a Bachelor of Jurisprudence degree and a Bachelor of Laws degree from the University of NSW, Australia and a Graduate Certificate in Management from the Monash Graduate Business School, Australia.

With Mr Leahy's term as President of the PNG Chamber of Commerce and Industry ending in November 2020, his term as a member of the Board of the Bank ended.

Bishop Denny Bray Guka

Bishop Denny Guka was appointed as an *ex officio* member of the Board in February 2012, in his capacity as President of the PNG Council of Churches.

He is the Bishop of the Anglican Diocese of Port Moresby and is Vice-Chairman of Anglicare PNG. He is a Director of the Papua New Guinea Medical Board and the PNG Bible Society and Vice-Chairman of Coronation Primary School.

Bishop Guka's educational qualifications include Certificates in Theology and in Teaching.

Mr Richard Kuna

Mr Kuna was appointed *ex officio* member of the Board in November 2015 in his capacity as the President of Certified Practising Accountants PNG.

He is a Partner with Kuna Taberia Kiruwi Accountants & Advisors. He is also a Board Member of the Accountants Registration Board of Papua New Guinea.

Mr Kuna has a Bachelor of Business in Accounting from the University of Technology, Sydney Australia and is a qualified Certified Practising Accountant.

Late Mr Simon Tosali OBE

Late Mr Tosali passed away in April 2020.

He had been appointed a *non-ex officio* member of the Board in March 2016 for a term of 3 years. He was reappointed for a further 3 years in March 2019.

He was also on the Board of Mineral Resources Development Company Limited.

Mr John Paska

Mr John Paska was appointed the President of the PNG Trade Union Congress in 2018 and by virtue of that appointment is an *ex officio* member of the Board. He is a labour advocate and a trade unionist.

Mr Paska also sits on the Boards of Security Industry Authority, National Tripartite Consultative Council and the National Training Council.

His education and expertise is in labour relations, trade and workers unionism and administration.

Governance

Mr David Toua

Mr Toua was appointed to the Board in February 2019 for a term of 3 years as a *non-ex officio* member.

As a very experienced business executive with comprehensive management and operational skills, he has served in various senior management executive positions in a number of corporate organisations.

He is Chairman of ABAC (APEC Business Advisory Council) and a Board member of the Business Council of PNG, the Employers Federation of PNG, the Mineral Resources Authority and Post PNG Ltd and an Advisory Board Member of the Royal Port Moresby Golf Club.

Mr Toua holds a Bachelor of Arts in English Literature, Economics & Government from the University of Queensland, Australia.

Board Meetings

The Board meets at least once every three months. The March 2020 Board meeting was held in Kavieng, New Ireland Province. Due to travel restrictions and other COVID-19 safety practices, the remaining Board meetings for 2020 were held in Port Moresby.

Board Member	Meetings Eligible to Attend	Meetings Attended
Mr Loi M. Bakani CMG	4	4
Mr Joseph Teria	4	4
Mr John Leahy	3	1
Bishop Denny Bray Guka	4	4
Mr Richard Kuna	4	3
Late Mr Simon Tosali OBE	1	0
Mr David Toua	4	2
Mr John Paska	4	4

Board Sub-Committees

The Board has established two sub-committees to perform specific functions for and on behalf of the Board. During 2020 the Committees were:

Board Audit & Governance Committee

The Board Audit & Governance Committee's primary responsibility under its Charter is to assist the Board to ensure the Bank's performance in financial reporting, internal controls, governance and risk management meets the required standards and expectations.

In line with best practice, the Committee comprised of non-executive directors. During 2020 Mr Richard Kuna was the Chairman of the Committee. The other members of the Committee were Mr John Leahy, Mr John Paska and Mr David Toua.

Board Remuneration and Succession Planning Committee

The Committee's primary responsibility is to assist the Board to determine the Bank's staff employment terms and conditions, in consultation with other relevant government agencies. It is also responsible for succession planning and for assessing the performance of the Governor.

During the year Mr John Leahy chaired the Committee, with Bishop Denny Guka, Mr Simon Tosali OBE and Mr John Paska as members.

Other Governance Measures

Internal Management Committees

Several internal management committees also continued through 2020, each with specific roles and responsibilities to ensure probity of the Bank's activities. They included the Executive Committee, the Monetary Policy Committee, the Currency Committee, the Investment Committee, the Tender Committee and the Budget Committee.

Internal Audit

A strong, independent and objective internal audit function is a key part of the Bank's overall commitment to good corporate governance practice. Over the course of 2020 the focus of internal audit was on several significant reviews and investigations, along with an ongoing program of routine audits. The Department also contributed to the Bank's Strategic Project on the Corporate Governance Framework Review.

Risk Management

In 2020 the Bank concentrated on the operational risk management function. Risk management activities undertaken during the year included business impact analysis, review of the Bank's business continuity management system, risk awareness and risk profiling for the Lae Currency Processing Facility (CPF) operations and several onsite risk assessments.

External checks and balances

As part of its commitment to good governance, the Bank continues to ensure there are external verification measures in its operation. These include:

Annual financial statements audit

Under the terms of the CBA 2000, the Auditor-General audits the Bank's financial statements every year.

Employment conditions

Staff employment terms and conditions are subject to approval by the Department of Personnel Management through the Salaries and Conditions Monitoring Committee.

The Governor's terms and conditions are subject to approval by the Salaries and Remuneration Commission.

Peer review

The Bank continues to maintain a practice of peer reviews with a range of organisations, including the central banks of Australia and New Zealand, the IMF, other regulatory authorities, such as the Australian Prudential Regulatory Authority (APRA) and through its membership of SEACEN and PFTAC.

Co-operation with Government Agencies

The Bank continues its relationships with other Government agencies in its operations, which help to mitigate the risk of fraud and other threats to the PNG financial and payments system.

Setting the right example

The Bank sets its expectations through the Values Statement, which provides clear guidance to Bank employees to conduct themselves with the highest standard of behaviour.

Financial Management

Operating Income

Total operating income for the year ended 31 December 2020 was K459.5 million, a decrease of K7.8 million from the 2019 level of K467.3 million. Revenue from financial assets, fees and commissions on foreign exchange trading increased by K24.4 million over the previous year. However, interest revenue from domestic investments declined by K32.2 million due to a reduced level of government securities holdings.

Operating Expenditure

Total operating expenditure, comprising interest expenses and general administration costs, was K328.6 million, an increase of K17.8 million from the 2019 level of K310.8 million. General and administration expenses increased by K3.1 million, while interest expenses increased by K14.7 million, mainly driven by an increase in domestic liabilities.

Net Operating Profit

The Bank recorded a net operating profit of K130.9 million for the 2020 financial year, compared to an operating profit of K156.5 million in 2019.

Unrealised Gain/(Loss)

The Bank recorded a net foreign and domestic financial assets revaluation gain of K302.9 million for the year ended 31 December 2020, which was transferred to the Unrealised Gain/(Loss) Reserve. This resulted from increases in bond prices and the depreciation of the kina against major currencies during the financial year. Gold valuation gain of K61.6 million was transferred to the Gold Reserve.

Appropriation

Under the CBA 2000, the Board of the Bank of Papua New Guinea in consultation with the Minister for Treasury determines the allocation of the Bank's operating profit, including the amount to be allocated to the Bank's retained earnings and any balance of net profit to be paid into the Government's Consolidated Revenue Fund (CRF).

However, the Board can decide that no amount is to be paid into the CRF if the assets of the Bank are less than the sum of its liabilities and paid-up capital, or would be, if a payment was made.

Furthermore, under Section 50(1) of the CBA 2000, net profit arising from revaluation of the Bank's assets and/or liabilities, and/or from foreign exchange rate movements shall not be made available for distribution as dividend to the Government or paid into the CRF.

Distribution of Profit

	2020 K'm	2019 K'm	2018 K'm	2017 K'm	2016 K'm
Total Comprehensive Income/(loss)	495.4	441.5	372.3	390.0	441.2
Unrealised Profit/(Loss)	364.5	285.0	185.1	216.2	270.7
DISTRIBUTABLE PROFIT/(LOSS)	130.9	156.5	187.2	173.8	170.5
ALLOCATIONS MADE:					
Property Revaluation Reserve	-	11.8	24.8	-	0.2
Unrealised Profits Reserve	302.9	236.9	155.3	193.1	251.5
Gold Reserve	61.6	36.3	5.0	23.1	19.0
General Reserve	-	30	-	-	-
Building Reserve	-	-	73.8	-	-
Retained Profit/(Loss)	(19.1)	6.5	13.4	73.8	70.5
Consolidated Revenue Fund (Government)*	150.0	120.0	100.0	100.0	100.0

** In 2020, in consultation with the Minister for Treasury, the Bank paid a dividend of K150 million to the Government.*

Income and Expenses

	Actual 2020 K'm	Actual 2019 K'm
Operating Income		
Interest received – overseas	128.4	136.6
Interest received – domestic	242.3	275.7
International trading/foreign exchange fees	69.3	36.6
Other income	19.5	18.4
TOTAL INCOME	**459.5**	**467.3**
Operating Expense		
Interest expenses – domestic operations	85.5	67.2
Financial markets & EFM expenses	8.4	11.9
Staff costs	105.5	87.6
Staff training and development	2.3	6.5
Premises and equipment	43.3	56.6
Depreciation of property and equipment	27.5	22.0
Amortisation of notes and coins production expenses	13.1	15.2
Currency distribution expenses	1.1	1.9
Audit fee	1.5	1.9
Travel	6.1	13.2
Legal & consultancy fees	6.5	6.9
Board & meeting expenses	1.2	1.9
Information & communication technology	9.6	-
Special projects	4.1	-
Other expenses	12.9	18.0*
TOTAL EXPENSES	**328.6**	**310.8**
NET OPERATING PROFIT/(LOSS)	**130.9**	**156.5**

** Includes information & communication technology and special projects.*

MONETARY POLICY

MONETARY POLICY FORMULATION

In 2020 the Bank released two monetary policy statements (MPS) that set out the six-month monetary policy stance as required by the Act, on 30 April and 30 September 2020. The delayed release of the first MPS was due to disruptions caused by the COVID-19 pandemic. With the pandemic causing data limitations and reduced coverage, the format of the MPS was shortened, and concentrated on major issues.

The MPS are available on the Bank's website: www.bankpng.gov.pg

The actual and projected developments in the international economy, domestic economic activity, balance of payments and fiscal operations of the National Government and their potential impact on monetary aggregates, the exchange rate, interest rates, and ultimately inflation were taken into account in the formulation of monetary policy.

On a monthly basis the Bank considers development in the same variables in setting the policy signalling rate, the Kina Facility Rate (KFR). Assessment of the quarterly Consumer Price Index (CPI) released by the National Statistical Office (NSO) and the monthly Retail Price Index (RPI) compiled by the Bank are key inputs into setting the KFR.

Throughout 2020 the Bank and Department of Treasury were engaged in consultative meetings to discuss estimates and projections of gross domestic product (GDP), balance of payments and inflation. These were used as inputs in the formulation of fiscal policy, especially the National and Supplementary Budgets, and monetary policy.

Annual headline inflation as measured by CPI increased to 4.9 percent in the December quarter of 2020, from 3.7 percent in 2019. Annual inflation was 3.1 percent in the March 2020 quarter, 6.0 percent in June, 5.8 percent in September and 5.1 percent in the December quarter.

The increase in inflation reflected the impact of the COVID-19 pandemic. The containment measures introduced to slow the progress of the virus disrupted the supply of seasonal produce, causing higher prices for fruits, vegetables and betelnut. Higher prices for medical services, medicines and education fees also resulted from the impact of COVID-19. These price increases outweighed low imported inflation.

The Bank introduced several policy measures in March and April 2020 aimed at mitigating the effects of the COVID-19 pandemic on the economy. The monetary policy stance was eased, with the KFR reduced from 5.0 percent to 3.0 percent. To ensure sufficient liquidity in the banking system, the Cash Reserve Requirement (CRR) was reduced from 10.0 percent to 7.0 percent and a Quantitative Easing (QE) program was introduced, allowing for holders of Government securities to sell their securities to BPNG before their maturity date.

Improvement in Monetary Policy Framework

During the year the work to implement the recommendations of IMF Technical Assistance to improve the transmission process continued.

MONETARY POLICY IMPLEMENTATION

Open market operations (OMOs) continued to be the main tool used to implement monetary policy during 2020. Following the reduction in the KFR in April 2020, moral suasion was applied to the commercial banks to reduce their indicator lending rates.

In the second quarter of 2020 the QE program through trading on the secondary market resulted in the purchase of a total of K724 million in Treasury bills and K25 million in Inscribed stocks from various investors, including commercial banks, superfunds and fund managers.

Other means of boosting liquidity in the market included reducing the CRR from 10.0 percent to 7.0 percent, which injected K643.5 million and an increase in the Repo margin by 25 basis points to 100 basis points on both sides and maturing some of the Bank's Central Bank Bills.

The Government faced cashflow challenges in 2020 due to the pandemic. It amended the *Central Banking Act 2000* in September 2000 to increase advances from the Bank. The TAF limit was increased from K300 million to K1.5 billion, to be repaid within twelve months. The utilisation of the TAF caused liquidity to exceed K2.0 billion.

The Bank retired most of its Treasury bill holdings (slacks and QE) maturing in 2020, with the goal of reducing exposure to State debt. Secondary Market trading was used to mop up liquidity. From its holdings, the Bank sold GIS stocks with a value of K603.4 million to a range of investors, including commercial banks, superfunds, fund managers as well as individual investors.

FOREIGN EXCHANGE

In 2020 the kina depreciated by 2.9 per cent against the US dollar, to close at US$0.2850 on 31 December 2021. The depreciation was mainly driven by persistent demand for foreign currency, which outweighed the supply in the domestic market. The market recorded a net outflow of K2,247 million in 2020, compared to a net outflow of K336 million in 2019.

Increased spending by the Government to support activity slowed by the pandemic was the main reason for increased demand for foreign currency. As this demand increased, the supply of foreign currency was affected by a slowdown in international trade, as lockdown measures and travel restrictions were imposed globally. The Bank intervened regularly to support the domestic foreign exchange market, by providing additional foreign currency liquidity. Despite BPNG's intervention, foreign exchange orders continued to remain elevated.

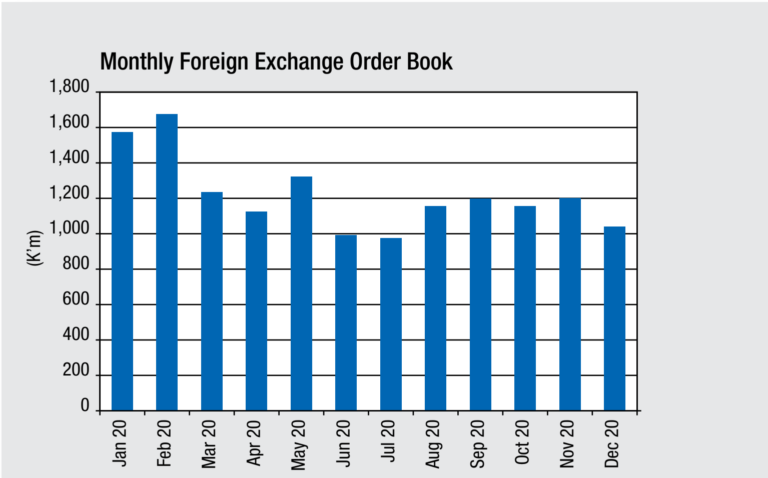
Foreign currency inflows decreased by 2.9 per cent while outflows increased by 9.1 per cent over the course of the year. The mining sector was the dominant supplier of foreign currency into the domestic market. The finance & business, manufacturing and retail sectors dominated the demand for foreign currency.

Major Sector Contributions to Foreign Exchange Flows

	2020 K'm	2019 K'm	Change
Total FX Inflows	**15,125.6**	**15,581.2**	**-2.9%**
Sectors			
Mining	6,211.7	5,863.7	5.9%
Finance & Business	1,889.9	2,201.8	-14.2%
Agriculture	1,806.6	1,896.7	-4.7%
Petroleum	920.9	1,296.9	-29.0%
Forestry	932.1	1,247.8	-25.3%
Total FX Outflows	**17,372.6**	**15,917.0**	**9.1%**
Sectors			
Finance & Business	3,671.3	3,338.9	10.0%
Manufacturing	2,644.2	2,594.0	1.9%
Retail	3,135.0	2,993.2	4.7%
Petroleum	1,690.6	1,742.5	-3.0%

Kina trading

Total outstanding sell kina orders brought into the market by Authorised Foreign Exchange Dealers (AFEDs) declined to K1.04 billion at the end of 2020, down from K1.56 billion at the end of 2019. Inflows from the mining sector and from external sources for budgetary support to the Government, particularly in relation to the pandemic, contributed towards reducing foreign exchange orders. BPNG's interventions also assisted in meeting some of the import demand.



Intervention

In 2020 the Bank sold US$579.6 million (K2,007 million) in the foreign exchange market. During the year the Bank's intervention was aimed at meeting foreign exchange demand, reducing outstanding foreign exchange orders and adhering to the IMF-recommended Staff Monitored Program (SMP) intervention benchmark.

Foreign Exchange Operational Guidelines

The Bank issued a Foreign Exchange Market Directive in July 2020 to suspend trading of forward exchange contracts (FEC) in the domestic foreign exchange market. The directive addressed issues relating to FEC pricing and behavioural issues by the AFEDs.

The Governor also approved the revised Foreign Exchange Operational Guidelines (FXOG) in December 2020, incorporating directives issued over the last 5 years and replacing the December 2015 version.

Exchange Rates

	End of Dec 2020	End of Dec 2019	YTD (%)
PGK/USD	0.2850	0.2935	-2.90%
PGK/AUD	0.3699	0.4188	-11.68%
PGK/EUR	0.2319	0.2619	-11.47%
PGK/GBP	0.2091	0.2238	-6.57%
PGK/JPY	29.39	31.9	-7.87%
PGK TWI	26.61	29.27	-9.09%

The kina depreciated against all the major currencies in 2020. The depreciation reflected a weaker US dollar mainly due to trade tensions and uncertainty surrounding the US Presidential elections.

Foreign currency and interest rates risks

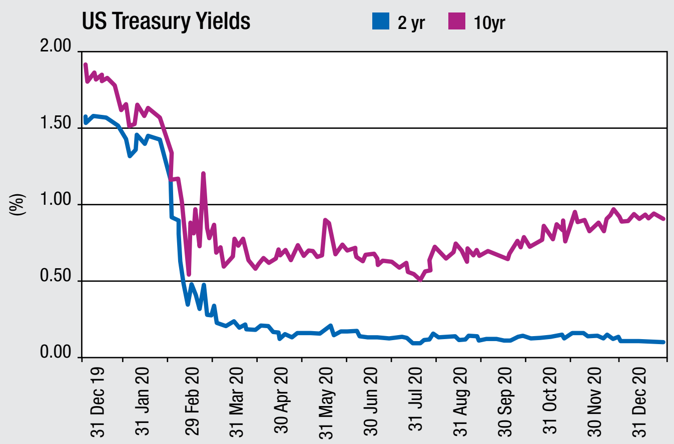
Global GDP growth contracted in 2020 as the COVID-19 pandemic weighed down economic activity. Business activity slowed as major economies enforced lockdowns and restrictions to contain the spread of the virus.

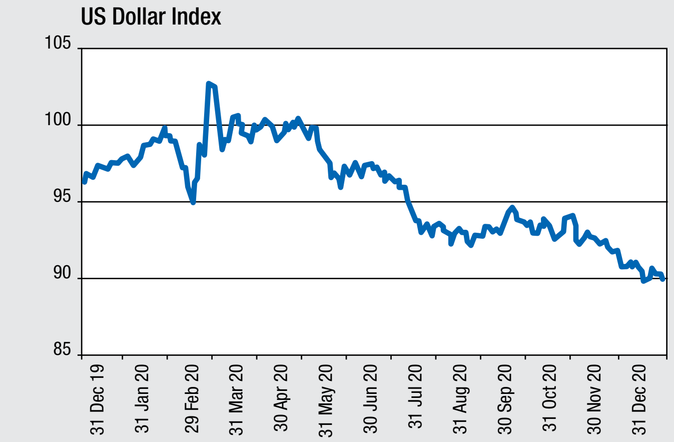
Employment and inflation declined worldwide, resulting from economic uncertainties, lower business confidence, stalled investment decisions and reduced global trade. However, while these developments undermined financial market sentiments, most advanced economies were supported by their governments' fiscal stimulus packages and accommodative monetary policy stances.

Interest rates in the US generally declined in 2020. The US Federal Open Market Committee reduced its Federal Funds rate twice to end the year at 0.25 percent. Similarly, the Bank of England and the Reserve Bank of Australia reduced their cash rates twice in 2020, both ending the year at 0.10 percent. Other major central banks kept their interest rates unchanged and maintained their accommodative monetary policy stances. Against this backdrop, bond yields in the US declined throughout the year.

The US dollar remained firm against other major currencies in the first quarter of 2020, but weakened in the final quarters due to the pandemic, continued trade tensions, uncertainty surrounding the US presidential elections and geo-political tensions.

In response to these market developments, the Bank of Papua New Guinea maintained an accommodative portfolio duration and currency exposure strategy throughout 2020.





FOREIGN RESERVES MANAGEMENT

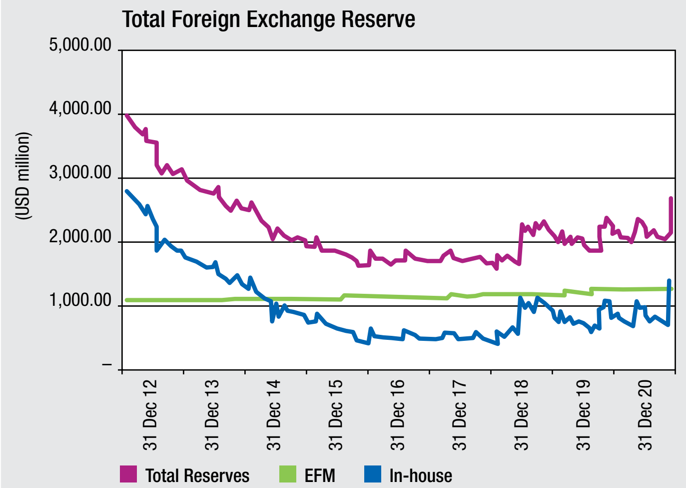
The Bank of Papua New Guinea is responsible for the management of PNG's international reserves, including foreign exchange and gold.

The main reasons for the Bank to hold foreign exchange reserves are to:

- support price stability (the core objective of the Bank's monetary policy)
- service the State's foreign debt
- minimise the impact of external shocks on the domestic economy.

In terms of investing foreign exchange reserves, the Bank's primary objectives are to:

- preserve the capital value of the foreign exchange reserves
- maintain adequate foreign currency liquidity
- manage credit risk conservatively
- earn an acceptable rate of return on the investment of reserves
- accumulate savings for the future generations.

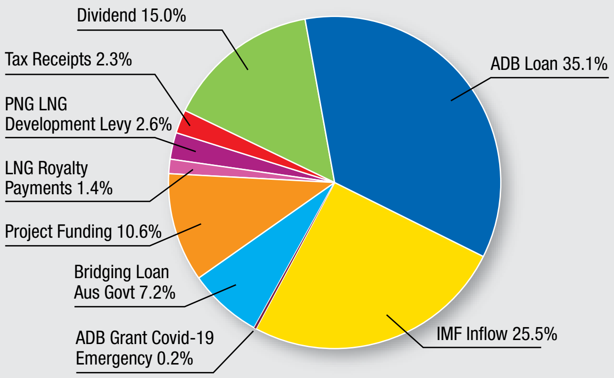


The total foreign exchange reserves at end December 2020 stood at US$2,709.35 million (K9,342.59 million), an increase of 15.88 percent from December 2019. The increase was mainly due to the inflow of soft loans from PNG's international partners. Under the conditions of the IMF SMP, from March 2020 BPNG had a minimum target level of foreign exchange reserves of US$1,800 million per quarter.

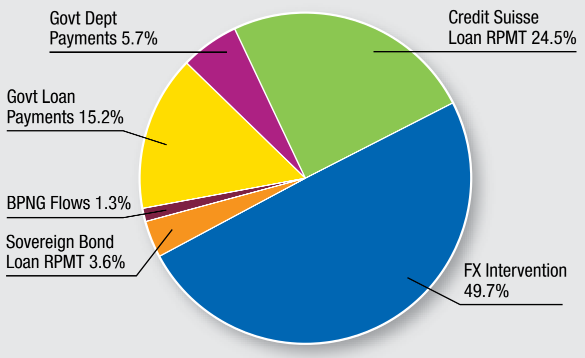
Composition of Foreign Exchange Reserves						
	In-house Managed Reserves	Externally Managed Reserves	Gold	Total Invested Foreign Reserves	IBRD	Total Foreign Exchange Reserves
Date	USD ('m)	USD ('m)	USD ('m)	USD ('m)	USD ('m)	USD ('m)
31 Dec 2020	1,373.84	1,254.30	80.96	2,709.10	0.25	**2,709.35**
31 Dec 2019	1,053.99	1,218.66	65.25	2,337.89	0.25	**2,338.14**
Change in US$	319.85	35.64	15.71	371.21	0.00	**371.21**
Change in %	30.35	2.92	24.07	15.88	0.00	**15.88**

Core Functions

Foreign exchange major inflows 2020



Foreign exchange major outflows 2020



Foreign exchange inflows totalled US$1,424.49 million in 2020, compared to total outflows of US$1,160.35 million, resulting in a net inflow of US$264.14 million.

Inflows mainly comprised:

- US$503 million ADB loan
- US$363 million IMF's Rapid Credit Facility support towards the COVID-19 pandemic
- US$213.85 million in dividends
- US$151.55 million project funding
- US$103.00 million bridging loan facility from the Government of Australia
- US$36.47 million LNG development levy and US$19.85 million LNG royalties
- US$32.95 million in mineral and petroleum taxes.

Outflows mainly comprised:

- US$576.89 million in domestic foreign exchange market intervention
- US$502.83 million in loan repayments
  - US$284.41 million Credit Suisse loan repayments
  - US$176.54 million to major government lenders
  - US$41.87 million in coupon payments for the sovereign bond
- US$65.76 million for PNG Government department payments.

Fund Performance

In-house Managed Funds

The Bank's in-house portfolio returned 3.5 percent for the 12 months to December 2020, outperforming the benchmark returns of 2.21 percent. All instrument types yielded positive returns. Commission from foreign exchange transactions was the main contributor to the returns, arising from large loan repayments from the reserves.

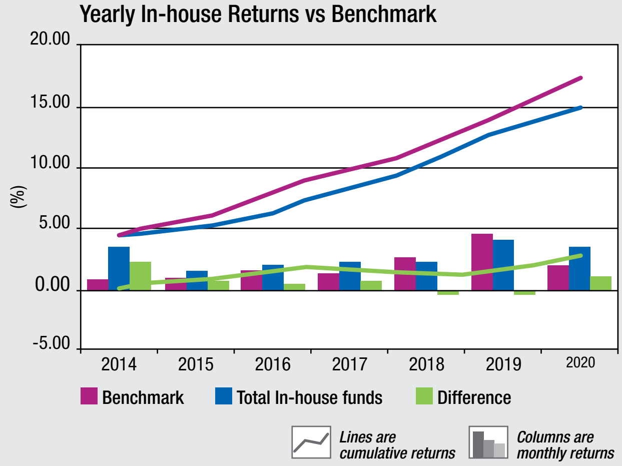
The COVID-19 pandemic caused a massive decline in yields across most of 2020. Some improvements in yields were observed towards the end of the year, as sentiment became more positive, responding to the resilience shown by economies withstanding the pandemic, along with news of vaccine development and roll-out. Valuation losses occurred in December.

In-house Funds Performance

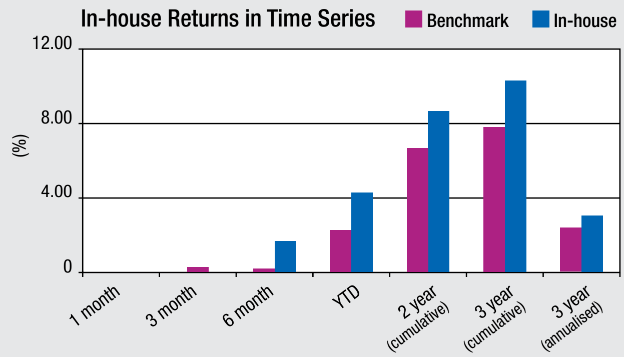
Performance for in-house reserves is calculated monthly and is measured against the FTSE Russell Government Bond Index 1 – 3 years USD Hedged.

In-house Funds – Comparative Performance to Benchmark

Yearly In-house Returns vs Benchmark



In-house Returns in Time Series



In-house Funds –
Comparative Performance to Benchmark (cont.)

	Return YTD	Benchmark YTD	YTD Difference
Dec 2020	3.52%	2.21%	1.31%
Dec 2019	3.04%	3.28%	-0.24%
Dec 2018	2.19%	2.06%	0.13%
Dec 2017	1.66%	0.92%	0.74%
Dec 2016	1.20%	1.18%	0.02%

Outsourced Funds

The outsourced funds generated a return of 2.92 percent, compared with 3.76 percent in 2019.

By December 2020 total outsourced funds had grown to US$1,254.26 million, an increase of 25.43 percent (US$254.26 million) since the inception of the outsourcing program in 2008.

Foreign Exchange Reserves Management – Annual Return (%)

Source	2020	2019	2018
In-house managed funds	3.52	3.04	2.19
Outsourced funds	2.92	3.76	1.97
Benchmark	2.21	3.28	2.06

International transactions monitoring

Foreign Currency Accounts

Opening and operating a domestic and offshore foreign currency account (FCA) requires BPNG's approval. During the year 13 new FCA applications were received. The Bank approved 4 applications and declined 9.

During 2020 the Bank conducted compliance checks to track monthly balances against the approved FCAs' three months transaction forecasts, to determine net credit or debit. The check reviewed 31 FCAs, resulting in amounts totalling US$49,321,641.12 and A$6,304,436.78 converted to kina.

The Bank also conducted compliance reviews on 14 FCAs during the year. Nine offshore and 5 onshore FCAs were found to be unauthorised. Six offshore and 5 onshore FCAs were closed, with closure of the other 3 offshore FCAs pending.

Gold export licences

Residents and non-residents are allowed to buy and sell gold freely within PNG. However, companies must obtain a licence from the Bank to export gold. Subject to complying with the conditions of the licence in each year, a new licence is granted to the licence-holder for the following year.

Applications Received in 2020	**19**
Licences approved	8
Mi-Do Gold Buyers & Exporters Limited Italpreziosi South Pacific Limited (ISPL) Aviga Impex Limited Golden Valley Enterprises Limited Issac Lete Lumbu Gold Buyers Limited Panners Gold Limited Enga Gold Exporters (PNG) Ltd New Guinea Five Star Metal Limited	
Applications declined	7
Applications cancelled	1
Applications requiring more information	3

Domestic lending in foreign currency

Lending by authorised dealers and other residents denominated in any foreign currency to PNG residents requires the prior approval of the Bank and their settlements must be in kina.

Application reviewed and declined in 2020	1
Value of transactions	US$11,850 million K41,578 million

Contingent Guarantees Issued in Favour of Non-Residents

The Bank's prior approval is required to issue guarantees (or indemnities) for the benefit of non-residents.

Applications received in 2020	11
Applications approved	10
Applications pending	1

Removal of Physical Cash from PNG

The Bank's prior approval is required to remove or take cash and numismatic banknotes in excess of K20,000.00 in value out of the country.

Applications received and assessed in 2020	9
Applications approved	7
Applications declined	2
Value of approved transactions	K499,540.84
Value of physical cash	K499,540.84
Value of approved numismatic notes exported	K0.00

FINANCIAL SYSTEM

The financial system of PNG includes institutions authorised, regulated and supervised by the Bank of Papua New Guinea ("regulated institutions") and financial institutions regulated by other authorities ("licensed institutions").

The Bank conducts prudential supervision of the regulated institutions to ensure stability of the financial system.

This is achieved through:

- setting licensing requirements
- promoting proper standards of conduct
- developing and issuing prudential standards and guidelines for sound and prudent business practices
- ensuring the institutions comply with the relevant legislations and prudential standards through effective supervisory activities.

The Financial System

Type of institution	31 Dec 2020	31 Dec 2019
Commercial banks	4	4
Licensed financial institutions including microbanks (LFIs)	14	14
Savings & loan societies (SLSs)	16	16
Authorised superannuation funds (ASFs)	4	4
Licensed investment managers (LIMs)	5	5
Licensed fund administrators (LFAs)	3	3
Life insurance companies (LICs)	4	4
Life insurance brokers (LIBs)	6	6
Authorised money changers	8	9
Money remitters	2	2
Foreign exchange dealers (AFEDs)	2	2
Authorised mobile network operators	1	1
TOTAL ASSETS (K billion)	**59.3**	**54.8**
Banking industry (%)	74.3	73.1
ASFs (%)	25.3	26.4
LICs (%)	0.4	0.5
TOTAL DEPOSITS (K billion)	**31.9**	**29.3**
Commercial banks (%)	94.0	93.6
LFIs (%)	2.8	3.2
SLSs (%)	2.5	2.5
Microbanks (%)	0.7	0.7
TOTAL LOANS OUTSTANDING (K billion)	**21.0**	**20.7**

REGULATION AND SUPERVISION

Licences and approvals

In 2020 the Bank considered and made decisions on several applications regarding acquisitions, expansion, closure, relocation of operations and new licences. During the year the Bank assessed 15 applications, of which 9 were approved and 6 are in progress.

February 2020

BSP Finance Limited advised the Bank that it had completed the settlement for a 50 percent stake in Davco Lao Leasing Company, a licensed leasing company in Laos.

March 2020

Kina Bank, Kina Ventures and Kina Properties were amalgamated into Kina Securities Limited. Kina Securities Limited is now the licenced entity trading as Kina Bank.

April 2020

Womens Micro Bank Limited (WMBL) set up a Mama Access Point (MAP) in Esa'ala District, Milne Bay Province in partnership with the Esa'ala District Development Authority.

June 2020

The Bank granted final approval of Nationwide Microbank Limited's (NMB) purchase of the Esi-Loan portfolio from Kina Bank. The sale and purchase was completed with the successful migration of data to NMB's core banking system in July.

December 2020

Westpac Group announced the proposed sale of its Pacific businesses to Kina Bank, pending the assessment and approval of the Bank and other regulatory agencies, including ICCC.

Supervisory enforcement actions

Reviews

The Bank conducts prudential reviews or examinations of regulated institutions as part of its supervisory role in strengthening their risk management systems and compliance capacity.

During 2020 the Bank's usual review program was curtailed, due to disruptions caused by COVID-19 pandemic. However, 1 onsite review was conducted.

The Bank also held 26 prudential consultations with 3 commercial banks, 9 licensed financial institutions and 14 savings and loan societies.

Supervisory Colleges

The Bank conducted two virtual supervisory colleges during the year, with ANZ Bank and BSP.

Employee Superannuation Contribution Enforcement

Onsite visits to provinces were suspended in 2020 due to the pandemic.

The Bank was enabled to commence prosecution against an alleged non-complying employer company and the company's owner as an individual, after a procedural error in the initial committal hearing led to the court's decision to instigate a judicial review and authorise a re-hearing.

By the end of 2020 the Bank had received 114 complaints from employees against non-complying employers. The Bank referred most of these complaints to be addressed by the relevant Authorised Superannuation Funds.

Statutory administration, management and liquidation activities

The interim board of the Central Bank Officers Savings and Loan Society, appointed in 2019, continued to address the transitional requirements of the Society set down in the *Savings and Loan Societies Act 2015*. In late 2020 the interim Board called for nominations for a new board and announced the shortlisted candidates.

Comrade Trustee Services Limited continues to be under statutory management in 2020.

The liquidation process for Workers Mutual Insurance (PNG) Limited and the Eastern Highlands Savings and Loan Society continued in 2020.

Regulation and supervision development

Risk-Based Supervisory Framework

The work on the enhancement of the risk-based supervision framework continued through 2020. During the year the focus was largely on risk profiling and rating of institutions and supervisory actions plans.

Directors Pipeline Project

As part of its commitment to helping regulated institutions to adhere to good governance practices, the Bank supported a development program for intending directors. During 2020 the first 7 participants completed the Post Graduate Diploma in Corporate Governance program at the University of Papua New Guinea.

Pacific KYC Facility

An initiative of SEACEN, with the concept launched at the South Pacific Governor's Meeting in November 2020, the aims of the regional 'Know Your Customer' facility ("Pacific KYC") include improving customer due diligence, reducing cost of remittances, lowering legal compliance risks and supporting correspondent banking services to the region. Compliance with anti-money laundering/counter terrorism financing processes is also a key objective of Pacific KYC.

The Bank participated in the development of a Pacific KYC regional guidance document and special case documentation for money transfer operators.

FINANCIAL SERVICES SECTOR DEVELOPMENT

Financial Consumer Protection framework

During the year the Bank continued work on the establishment of the Financial Consumer Protection supervision framework in consultation with the International Finance Corporation (IFC).

SME Accelerator Project

The SME Accelerator project, established to address the barriers to SME growth in PNG, continued through the year. The focus of activities in 2020 on access to finance, in particular, the creation of a credit guarantee system that would operate in partnership with commercial banks and other selected financial institutions.

The Bank sought legal advice on the incorporation of an independent legal entity, the Credit Guarantee Corporation.

Integrated prudential regulation of the insurance sector

The Bank held discussions with the Department of Treasury and the Office of Insurance Commissioner during the year, resulting in agreement for life insurance and general insurance regulatory functions to be amalgamated within BPNG.

Secondary bond market development

Work to establish an exchange-traded secondary market for government securities progressed during 2020, with market arrangements including the agreed new debt market rules.

Financial education in schools

The Department of Education responded favourably to a concept note from the Treasurer to the Minister of Education. As a result, the Centre of Excellence for Financial Inclusion (CEFI) and the Department of Education signed a Memorandum of Understanding relating to incorporating financial education into the education curriculum.

PAYMENT SYSTEM

NATIONAL PAYMENT SYSTEM

The National Payment System (NPS) is part of the core financial infrastructure that supports the PNG economy. The Bank of Papua New Guinea holds responsibility for the NPS, in line with the *National Payment System Act 2013* ("NPS Act").

The Kina Automated Transfer System (KATS) was developed to implement the NPS, to meet the aim of delivering money from payer to payee, effectively and efficiently. The Bank's other NPS responsibilities include currency management and agency services.

The major achievement for NPS during 2020 was maintaining operations throughout the year in spite of challenges arising from the COVID-19 pandemic, such as significant restrictions on normal staffing arrangements.

The combination of KATS and the Retail Electronic Payments System (REPS) proved reliable and successful throughout the year, even though demand for electronic payment options for retail purchases increased and transaction volumes grew, in response to strict rules aimed at minimising physical contact.

The Bank's payment system development achievements were recognised in February when BPNG, in conjunction with the World Bank, hosted a 3 day seminar. Representatives from the central banks of the Solomon Islands, Vanuatu and Fiji who attended the seminar were able to see payments operations in action as well as participate in discussions about daily operations and development planning.

REPS development

A number of development projects were put on hold during 2020, while the Bank's focus was on ensuring uninterrupted operations.

However development of the REPS program continued, with work on linking existing services and improving access to digital payments, including the facility to make instant payments.

The REPS project team also supported People's Microbank Limited as they added acquiring capabilities at their ATMs in December. The enhancement allows customers of other REPS member institutions to use their cards at PMBL ATMs for withdrawals and balance enquiries.

National Payments Council

The National Payments Council was established as a strategic forum and advisory body to the Bank, representing all major players in the market and relevant public bodies.

During 2020 the National Payments Council held two meetings. In February the meeting discussed planned developments as well as hosting representatives from Pacific central banks visiting BPNG as part of the payments seminar.

At the meeting in December the Council discussed the fees structure for the new REPS payments and the strategic direction of payment system developments for 2021 and 2022.

Payment type trends

The use of real time payments and direct credits continued to increase strongly over the course of 2020. Use of cheques continued to decline significantly.

Volumes by Payment Type

Year	RTGS	Cheques	Direct Credits
2016	70,372	1,419,753	2,419,273
2017	80,067	1,222,793	2,663,180
2018	96,857	1,073,319	3,062,576
2019	108,887	959,876	3,508,368
2020	105,488	705,048	3,958,155

Values by Payment Type

Year	RTGS	Cheques	Direct Credits (K'm)
2016	52,027	34,319	16,846
2017	42,972	28,356	18,740
2018	84,360	26,242	26,683
2019	98,102	23,460	31,052
2020	105,248	19,135	32,121

CURRENCY MANAGEMENT

Currency banknotes and coins

One of the Bank's key responsibilities is to issue currency notes and coins. This role involves ensuring an adequate supply of quality currency in circulation, withdrawing damaged and soiled banknotes from circulation and monitoring the overall supply of currency.

Currency distribution

The Bank distributes cash from its head office in Port Moresby and from the Currency Processing Facility (CPF) in Lae, Morobe province. It also distributes from the Cash Distribution Centre in Kokopo, East New Britain province.

Currency in circulation

By the end of 2020 the value of currency banknotes in circulation had increased to K2,338.2 billion (2019: K2,208.9 billion), while the value of coins in circulation had increased to K95.9 million (2019: K91.9 million).

Total currency in circulation by 31 December 2020 amounted to K2,434.1 billion (2019: K2,300.8 billion). The K133.4 million increase was mainly due to higher demand for K100, K50 and K2 denominations by the commercial banks. There was also a slight increase in demand for most coin denominations.

Notes and Coins in Circulation

Notes Denomination	Value (K'm) 2020	Value (K'm) 2019
K2	67.4	62.1
K5	60.6	64.0
K10	80.3	87.5
K20	217.9	217.1
K50	593.7	559.9
K100	1,318.3	1,218.3
Sub Total	**2,338.2**	**2,208.9**
Coins Denomination		
K2*	0.2	0.2
K1	32.3	30.3
50 Toea	8.5	8.1
20 Toea	23.9	22.9
10 Toea	23.9	23.3
5 Toea	7.3	7.1
Sub Total	**95.9**	**91.9**
Total	**2,434.1**	**2,300.8**

** No longer issued*

New notes and coins

The Bank issued new notes and coins in 2020 to the value of K791.25 million (2019: K909.9 million). The decline was mainly due to a decrease in currency demand for most denominations as a result of the pandemic and increased usage of electronic payments.

Notes Denomination	Value (K'm) 2020	Value (K'm) 2019
K2	26.5	25.9
K5	16.5	26.0
K10	30.1	37.5
K20	128.4	119.6
K50	216.9	272.5
K100	365.4	417.0
Sub Total	**783.7**	**898.5**
Coins Denomination		
K1	4.36	8.62
50 Toea	0.41	0.48
20 Toea	1.97	0.48
10 Toea	0.69	0.97
5 Toea	0.12	0.32
Sub Total	**7.55**	**11.36**
Total	**791.25**	**909.86**

Destruction of Soiled Notes

Notes Denomination	Value of Soiled Notes destroyed (K'm) 2020	Value of Soiled Notes destroyed (K'm) 2019
K2	21.0	30.1
K5	20.3	26.1
K10	35.8	38.3
K20	87.9	113.3
K50	211.1	248.9
K100	286.2	289.0
Total	**626.3**	**745.7**

Numismatic items

The Bank sells commemorative items to the public and currency collectors worldwide. Total value of sales was K0.1 million in 2020 (2019: K0.9 million). The decrease was attributed to the negative impact of the COVID-19 pandemic.

The 2018 APEC K100 gold coin, the K2 note and coin pack, the 50 toea St Johns coin set and the 2015 UPNG K5 coin, as well as uncirculated numismatic banknotes, continued to be popular, in spite of the downward pressure on sales.

GOVERNMENT BANKING AND AGENCY SERVICES

The Bank of Papua New Guinea provides banking services to the National Government and other authorities as part of its statutory function.

The financial activities of the National Government are conducted by the Department of Finance through the Waigani Public Account, from which transfers of funds are initiated and executed to the various national government departmental drawing, trust and provincial government and statutory authority accounts.

The Government maintained 45 drawing accounts for national departments and 98 trust accounts with the Bank during 2020. The balance of the trust accounts at 31 December 2020 was K861 million (2019: K519 million), with most of the funds held in the trust accounts for PNG LNG Royalties (K412m), Connect PNG Economic Road Transport (K133m), PNG LNG Development Levies (K124m) and Tuition Fee Free Education (K87m).

As part of the National Government's Integrated Financial Management System (IFMS), drawing accounts for the provinces and districts were held at the Bank. Large transactions processed during 2020 through IFMS accounts related to provincial and district services improvement projects, provincial and district grants, Tuition Fee Free Education, Autonomous Bougainville Government grants, medical supplies and COVID-19 related expenses and infrastructure development projects coordinated by the Department of Works and Implementation and the Department of National Planning and Monitoring.

During 2020 all organisations and business entities made their tax and customs payments through KATS to IRC and PNG Customs accounts maintained at the Bank.

Improvements to cheque processing, including cheque truncation, standardising cheques and automated clearance, continued to prove effective and secure throughout 2020.

Banking services development

Over the course of 2020 the Bank continued to hold discussions and co-ordinate activities with Department of Finance to further improve banking services provided to the Government, including ensuring compliance with Anti-Money Laundering legislation requirements.

Temporary advance facility

The National Government operates a Temporary Advance Facility (TAF) with the Bank to meet short-term cash flow mismatches during the year in accordance with the CBA 2000. In August 2020 the TAF limit was increased from K200 million to K300 million.

Responding to the cashflow challenges arising from the COVID-19 pandemic, the Government amended the CBA 2000, effective from 4 November 2020, to change the method of calculating the TAF limit to 12 percent of the average revenue and grants of the preceding 3 years and extending the term from 6 months to 12 months.

In line with the amendment, the revised TAF limit for 2020 was set at K1.5 billion.

During 2020 the Government sought financing under the facility at a similar level of frequency as in the previous year.

Debt repayment account

The Government also operates a Debt Repayment Account separate to the Waigani Public Account, specifically to cater for immediate debt servicing requirements. The closing balance at 31 December 2020 was K314 million (2019: K1m).

Government Agent Operations

The Bank of Papua New Guinea is the Agent for the National Government as an authorised issuer, registrar and paying agent for Government securities.

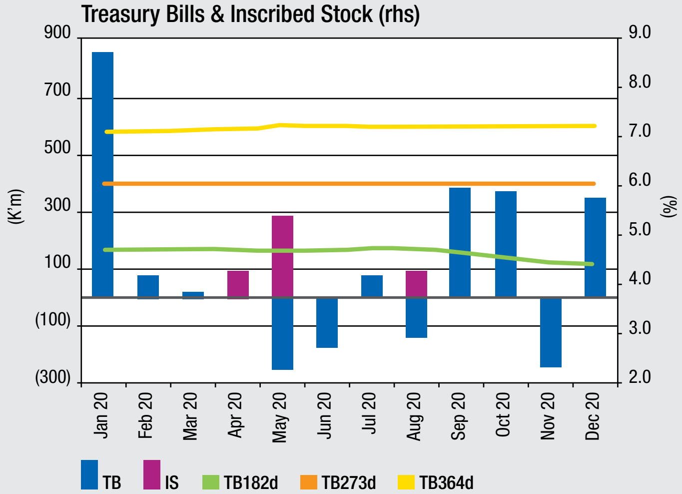
The Bank is also a member of the Government's Public Debt Committee (PDC). Representatives from the Bank attend the weekly PDC meetings convened by the Department of Treasury.

Treasury bill and Treasury bonds (Inscribed stock)

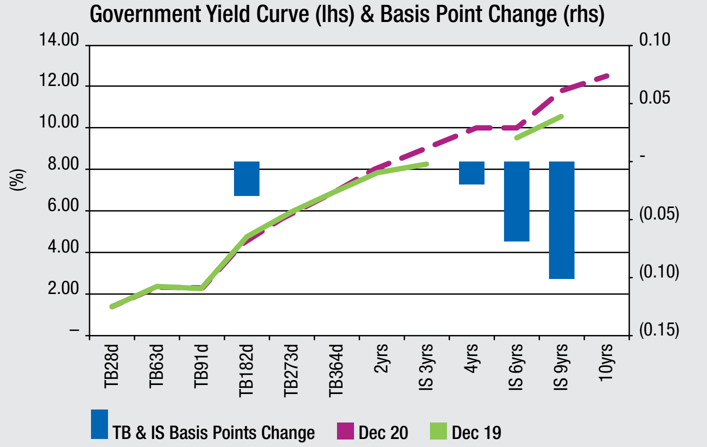
The Bank continued to consult closely with the Government on matters concerning the coordination of budget financing. In 2020 the Government issued its Treasury bills (T bills) mainly in the 182, 273 and 364 day terms. The Treasury bonds (T bond, Inscribed stock [IS]) were issued in the 2, 3, 4, 5, 6 and 10 year terms. The Government's issuance strategy for T bill holdings was mainly re-investing maturities and for T bonds, was issuing long-term Covid 19 bonds in line with the National Budget.

The interest rates for most T bills and T bond terms generally remained stable due to high liquidity. The T bills and T bonds were generally oversubscribed, reflecting an increase in demand. The Government conducted only three IS auction during the year in April, May and August.

Average Net Subscription Volumes (lhs) & Interest Rates – Treasury Bills & Inscribed Stock (rhs)



Government Yield Curve (lhs) & Basis Point Change (rhs)

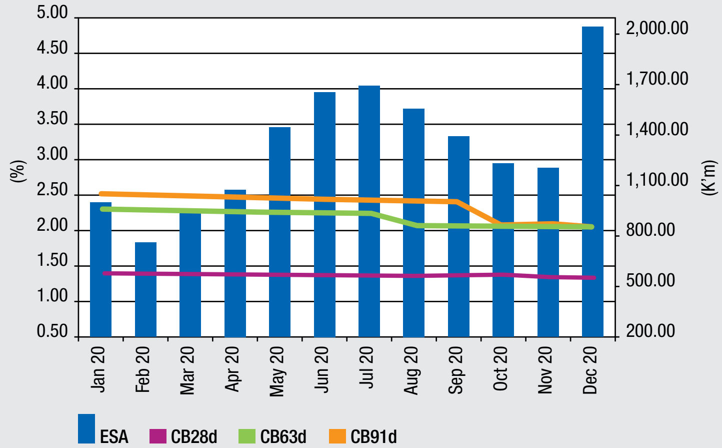


Central Bank Bills

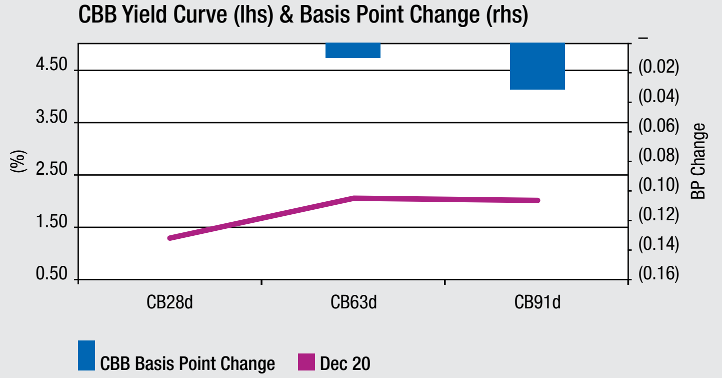
The Bank issued its Central Bank Bills (CBBs) mainly in the shorter-dated terms, 28 days, 63 days and 91 days. In 2020, the CBB interest rates remained stable. CBB auction demand was mostly over-subscribed, reflecting moderate demand.

Banking system liquidity, as measured by the Exchange Settlement Account (ESA) balances, averaged around K1,333.0 million, K373 million above the 2019 level. The increase in ESA level reflected the impact of retirement of CBBs, the Quantitative Easing measure, the reduction in CRR and the increase in TAF limit.

CBB Average Interest Rates (lhs) & ESA (rhs)



CBB Yield Curve (lhs) & Basis Point Change (rhs)



Tap facility

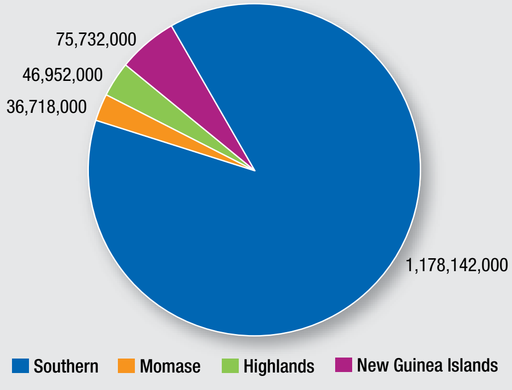
The CBB Tap facility aims to encourage investment by individuals, to help develop a savings culture within PNG. It provides an opportunity for individuals and small businesses, ineligible to participate at the primary auctions, to invest in government securities.

Trading in the Tap facility continued throughout 2020. Under the facility, both T bills and T bonds were offered with a minimum investment of $5,000.00. T bills were offered in shorter dated terms of 63, 91, 182, 273 and 364 days. T bonds were offered in longer dated terms of 2, 4, 8 and 10 years, with the 10 year T bond the most preferred.

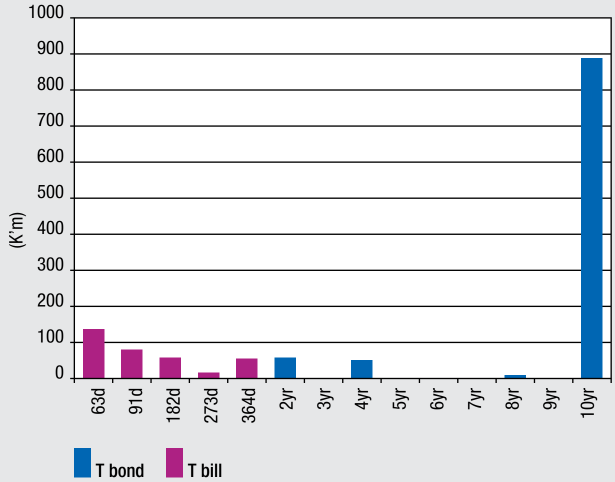
Total sales by the end of 2020 were K864.1 million, a dramatic 80.3 percent increase over the previous year (2019: K479.3 million).

The strong result was attributed to favourable interest rates and the efforts of Bank staff, who distributed the Bank's donations of personal protective equipment to rural health centres and clinics in East Highlands, Jiwaka, Western Highlands, Milne Bay, West Sepik, Morobe, Manus and New Ireland provinces, at the same time creating awareness of Tap investments.

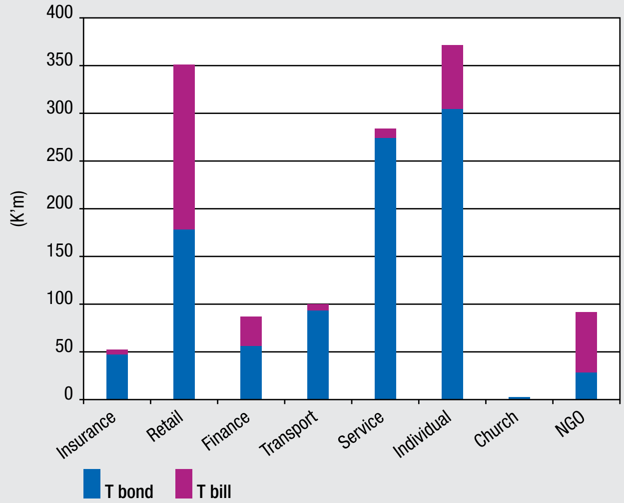
Tap Sales by Region as at 31/12/2020

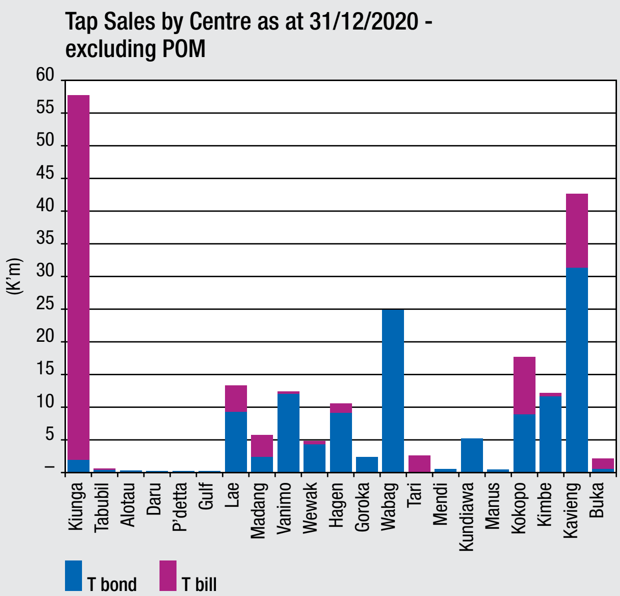


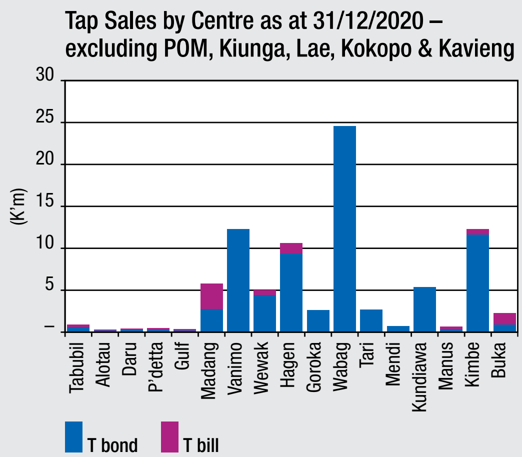
Tap Sales by Term as at 31/12/2020



Tap Sales by Sector as at 31/12/2020







"Slack" arrangement

With the ending of the slack arrangement between the Bank and the Department of Treasury in 2018 and no slack taken up in 2019, the Bank retired its T Bills slack holdings in 2020. At the end of the year the total holdings of slacks had declined to K32.36 million.

Secondary market activity

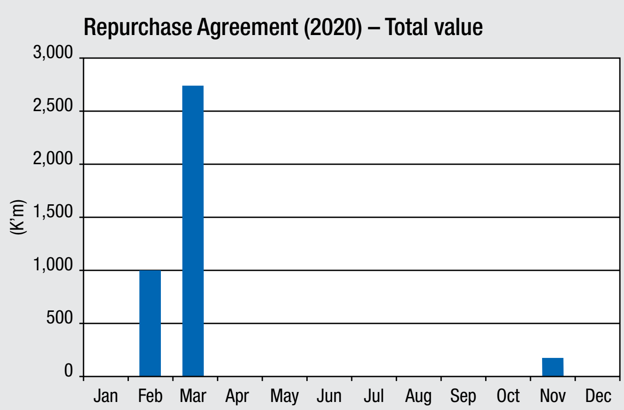
The Bank sold a total of K603.4 million of its T bond holdings to investors on the secondary market.

The Bank's Quantitative Easing program also utilised the secondary market between April and June 2020, with the Bank buying Government securities from holders, then holding the stock until maturity.

Collateralised Repurchase Agreement facility

The Bank introduced the Collateralised Repurchase Agreement facility in 2019. The effect of the facility is to secure lending to commercial banks by buying outright a nominated security asset (either T bill or T bond) and repurchasing at a predetermined maturity date. The ownership of the security transfers to BPNG at the first stage and reverses at the second stage after successful repayment at maturity by the commercial bank. These transactions generate interest income for the Bank.

During the year 39 repurchase contracts were completed, with a total value of K4 million, significantly lower than the K15,112 million transacted in 2019.



Government debt

By the end of 2020 total borrowing by the Government from the public amounted to K21.1 billion (2019: K18.2 billion). The borrowing comprised of K9.2 billion in Inscribed stock and K11.9 billion in T bills. Of this, BPNG holds K1.4 billion.

Treasury bills

	K'm
Outstanding as at 31 Dec 2019	10,191
Issued in 2020	13,148
Slack Issued 2020	0
Maturities in 2020	11,437
Slack Maturities in 2020	0
Net Issuance	1,711
Outstanding as at 31 Dec 2020	11,902

Treasury bonds (Inscribed stock)

	K'm
Outstanding as at 31 Dec 2019	7,967
Issued in 2020	2,567
Maturities in 2020	1,301
Net Issuance	1,266
Outstanding as at 31 Dec 2020	9,233

BPNG Holdings T bills and Holdings

	K'm
BPNG Holdings 31 Dec 2019	2,010
Net Maturity in BPNG Holdings	576
BPNG Holdings 31 Dec 2020	1,434

Central Bank Bills

	K'm
Outstanding as at 31 Dec 2019	1,301
Issue in 2020	9,635
Slack Issued in 2020	0
Maturities in 2020	10,183
Slack Maturities in 2020	0
Net Maturity	548
Outstanding as at 31 Dec 2020	753

BPNG Bill Tap facility

	K'm
Outstanding as at 31 Dec 2019	32
Issued in 2020	81
Maturities in 2020	74
Early Redemption	0
Net Issuance	7
Outstanding as at 31 Dec 2020	39

BPNG Bond Tap facility

	K'm
Outstanding as at Dec 2019	448
Maturities in 2020	19
BPNG Bond Early Redemption	60
Issued In 2020	457
Net Issuance	378
Outstanding as at Dec 2020	826

Secondary Functions

ECONOMIC ADVICE TO GOVERNMENT

The Bank of Papua New Guinea provides the National Government with economic advice to help optimise fiscal and economic policy. The Governor is required to advise the Treasurer of the effect Government policy may have on monetary policy.

The Governor or his representatives provide economic advice through presentations at various official forums and the Governor's 6 monthly Monetary Policy Statements. Bank staff also present economic information at technical meeting attended by officers from the Department of Treasury and other Government departments.

In accordance with the CBA 2000, special reports must also be provided to the Minister on adverse conditions that threaten the country's monetary stability, affect monetary policy or the economic and financial policies of the Government.

INCREASING ECONOMIC KNOWLEDGE

Research activities within BPNG are key to increasing economic knowledge, as well as aiding policy analysis, decision making and forecasting, which are essential in preparing the Bank's six-monthly Monetary Policy Statement.

While the COVID-19 pandemic restricted a number of research projects during the year, the Bank continued to perform a range of activities, including information gathering through PNG-wide industry surveys, producing research papers, both in-house and in collaboration with Griffith University, Australia.

Research topics considered during the year included:

- assessing the impact of the pandemic on the Bank's balance sheet
- forecasting the output gap
- modelling the exchange rate and inflation
- stress-testing key banking and financial system stability indicators, to assess the impact of the pandemic on the financial system.

The findings of the nation-wide Business Liaison surveys are essential inputs for the Bank's 6 monthly Monetary Policy Statements and key information for GDP forecasts for the Government's national budget. The survey covers a sample of 366 major companies in the private sector, representing 80 percent of all businesses in PNG, across various industries and from a wide geographic spread. During the year the survey was redesigned to take account of the impact of the pandemic on businesses, including impact on sales.

In 2020 the Bank conducted a business pulse survey through the SME Accelerator Program to determine the impact of the COVID-19 pandemic on SMEs. The survey involved over 1,700 SMEs, on-site visits to 13 provinces and online contact with SMEs from other provinces.

FACILITATING FINANCIAL SERVICES DEVELOPMENT AND INCLUSION

As well as carrying out its three core functions, the Bank of Papua New Guinea actively supports and contributes to the Nation's economic growth.

The main focus in this area is the Bank's commitment to the successful completion of the National Financial Inclusion Strategy 2016 – 2020 (NFIS 2), in particular with its close working relationship with the Centre of Excellence in Financial Inclusion (CEFI).

2020 key financial inclusion results

	End 2020	End 2019
Total number of deposit accounts	3,301,496	3,259,843
Access points	14,205	14,050
Branches	221	228
ATMs	473	471
EFTPOS merchants	13,099	13,032
Agents	412	327
Mobile financial services accounts	848,695	739,115

The Centre for Excellence in Financial Inclusion (CEFI)

CEFI is the apex organisation responsible for coordinating all financial inclusion activities in PNG, including the implementation of the National Financial Inclusion Strategy 2016 – 2020 (NFIS 2), the nation's second financial inclusion strategy.

The Strategy identifies 9 priority areas for support to expand financial inclusion:

1. Digital Financial Services
2. Inclusive insurance
3. Financial Literacy and Financial Education
4. Financial Consumer Protection*
5. Informal Economy and Agricultural Finance
6. SME Finance
7. Resources Sector Engagement (mining areas)
8. Data Collection and Dissemination
9. Government Engagement

****With the development of the framework to provide financial consumer protection, the work of this group was concluded.***

2016-2020 Financial inclusion strategy

NFIS 2 provides the blueprint through which the Financial Inclusion Policy launched in 2019 can be achieved.

Strategy rollout activities

With COVID-19 restrictions preventing in-person meetings, in 2020 meetings were held online by working groups Digital Financial Services, Financial Literacy & Financial Education, SME Finance, Inclusive Insurance and Access to Finance for Informal and Agricultural Enterprises.

2020 Financial Inclusion Highlights

(Acknowledgement: information sourced from CEFI)

- CEFI signed the partnership memorandum with Fresh Produce Development Agency (FPDA) under the Market for Village Farmers (MVF). The Project aims to deliver financial inclusion products and services as well as family farm team training to 25,000 fresh produce farmers in six provinces.
- CEFI delivered the first ever 2-day Digital Finance Symposium in PNG via online platforms. The Symposium reached over 300 local and international participants.
- PNG through CEFI acquired the Microfinance Pacifica Network. CEFI will assume the role of the secretariat to lead important financial inclusion initiatives in the region.

- CEFI and the National Training Council discussed forming a partnership to improve financial literacy training modules in the country.
- CEFI and National Volunteer Service signed Financial Literacy Training MoU for CEFI to deliver training for national volunteers in communities.
- CEFI and APEC Secretariat collaborated to implement fintech incubator for innovative approaches for financial inclusion in PNG.

FINANCIAL INTELLIGENCE MONITORING

The Financial Analysis and Supervision Unit (FASU) is PNG's Financial Intelligence Unit (FIU). FASU is an operationally independent unit established by legislation in the Bank of Papua New Guinea. Its role is to coordinate efforts to protect PNG and the integrity of the PNG financial system against money laundering and counter terrorist financing (AML/CTF) and other serious financial crimes.

AML/CTF activities in 2020 were hampered by the COVID-19 restrictions. Only 1 onsite inspection of a financial institution was conducted. Offsite supervision efforts through desktop reviews from responses received were conducted on 2 commercial banks, 2 non-bank licenced finance institutions, 4 money changers, 4 motor vehicle dealers and 1 law firm. A financial institution submitted a self-disclosure report for non-compliance. FASU is working with the institution to rectify and resolve the issues reported.

FASU signed information sharing arrangements with 3 domestic agencies during the year. By the end of 2020 FASU held agreements with 15 international FIUs and 14 domestic agencies.

In line with the recommendations from the Financial Action Task Force (FATF), the global money laundering and terrorist financial watchdog, FASU continues to share information with domestic agencies and internationally, through FIU membership of the Egmont Group, a global network of more than 170 FIUs.

Institutional Support

STRATEGIC AND OPERATIONAL MANAGEMENT

Risk Management

2020 was a very challenging but important learning year for risk management. Disruptions to the workplace early in the year, resulting from air conditioning system breakdown, followed by the major impact of the COVID-19 pandemic, meant the Bank had to invoke and implement a Business Continuity Plan (BCP) and learn to deal with issues that affected all staff and virtually all business processes.

During the year the Bank had to operate in crisis mode, maintaining essential services at all times for an extended period, made even more difficult with uncertainty about the pandemic within PNG and on a global level.

Working from Home (WFH) became the 'new norm' for the Bank. The WFH solution also created additional risks to data security and cyber risk as the Bank granted remote server access, facilitated video conferencing calls and other potential threats to privacy.

The Bank also had to take on additional occupational health and safety risks for both essential staff who came into the office and the majority of staff whose WFH environment may not have been ideal.

The COVID-19 BCP had a number of positive outcomes. It prevented the Bank from getting stuck on "silo thinking" in the context of risk management. For the Bank to meet the objective of ensuring essential services, departments needed to commit to teamwork and collaboration throughout the organisation.

The Strategic and Risk Management Office (SRMO) initiated the Enterprise Risk Management Framework (ERMF) and Business Continuity Management (BCM) Reviews to enhance an enterprise-wide risk management framework and also establish and improve the BCM System.

Strategic Management

Strategic initiatives, programs and business improvement projects

The Bank reviewed its project portfolio in the light of the impact of the pandemic and the capacity and resources of the Bank while operating under the BCP. All non-critical projects were put on hold. Critical projects whose resources were not affected by the pandemic continued. The scope of most projects and delivery timeframes were adjusted.

Being the final year of the Strategic Plan Period for 2016 – 2020, no new projects were initiated in 2020. The focus was on consolidating 'inflight' projects and projects in the closure phase and near transition to business as usual.

Key achievements in 2020 included:

- automated the records management system
- established the Gender Equity and Social Inclusion function
- developed and established Financial Consumer Protection as a new function
- opened the Lae Currency Processing Facility (CPF) Staff Accommodation
- commissioned a new printing office at Badili, Port Moresby
- upgraded the security systems
- completed two office fit-outs.

Strategic and Risk Management Office team

L-R: Darren Douglas, Beverley Mirou, Tracey Leko, Annfrances Camilus and Nathan Maire.

HUMAN RESOURCES MANAGEMENT

Staff numbers

Staff Category	2020	2019	2018
Non-management level staff	457	462	417
Management	63	63	59
Executive	7	6	6
Total	527	531	482

Staffing

The Bank's staff complement decreased to 527 in 2020, down from 531 in 2019. Recruitment was put on hold in response to the pandemic.

Employee capacity development

The pandemic posed numerous challenges for capacity building at the Bank in 2020. Over the course of the year the Bank maintained sponsorships for employees to attend training programs related to their roles. These included workshops, conferences, short courses and longer term formal studies, with virtual learning largely replacing face-to-face sessions.

The Bank has long recognised the benefit of continuous affiliation with professional bodies, to maintain its network and the professional standing of its employees, and continues to encourage staff to hold memberships from relevant industry associations. Due to COVID-19, only local short courses were attended by staff (face-to-face learning), including two outbound Leadership & Management refreshers in November.

Most of the planned training programs with SEACEN and the IMF were cancelled. The Bank was also unable to utilise funds from the SEACEN Trust Fund Scholarship (STFS) scheme, which were returned to the STFS.

Apart from virtual learning, the Bank continued with its structured capacity development programs for employees. Such programs include supervisory and management skills, employee engagement workshops, leadership and communication skills for staff.

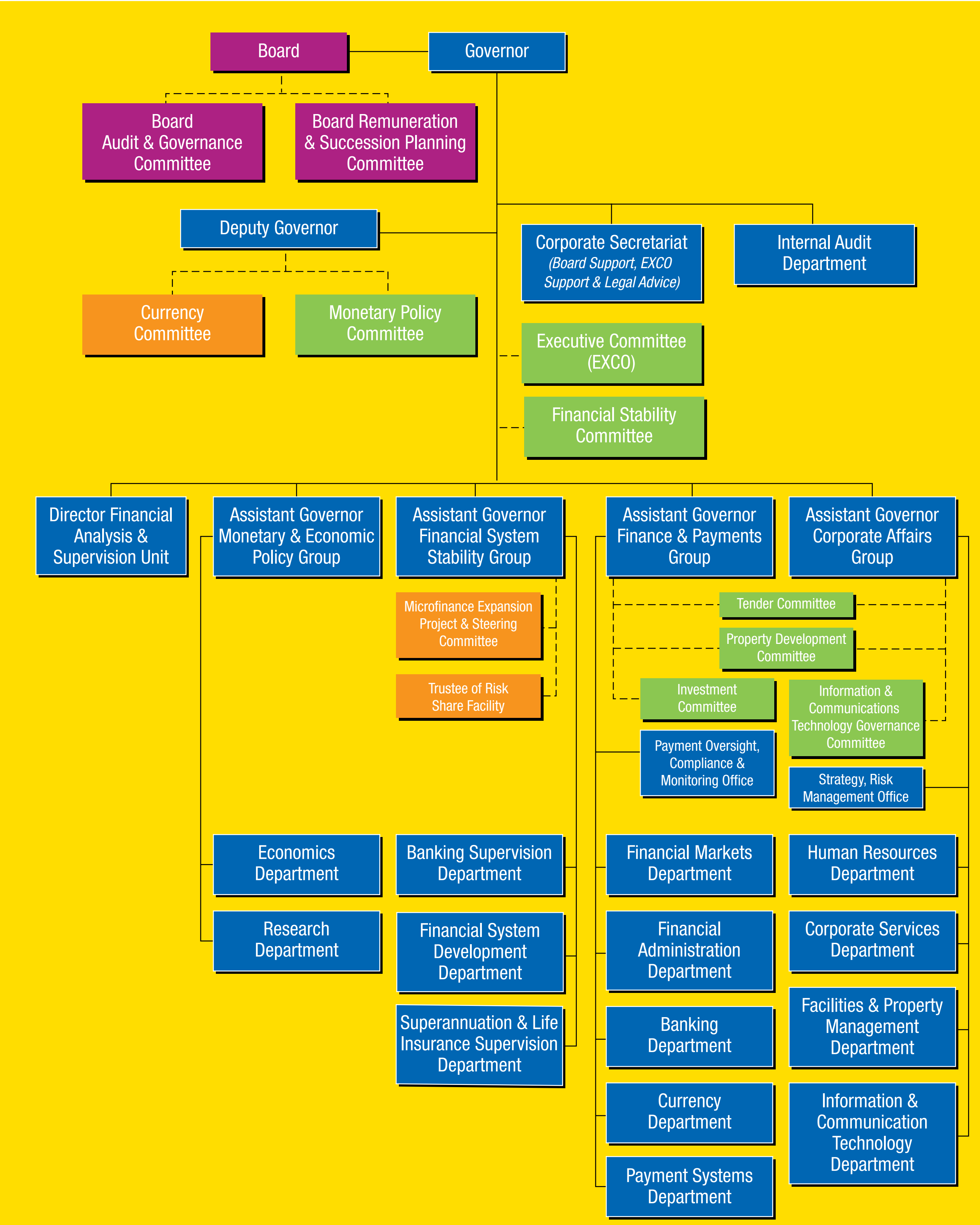
Gender Equity and Social Inclusion (GESI)

In 2020 the focus turned to the issue of family and sexual violence (FSV). The Bank's GESI Focal Points attended a train-the-trainer session on family and sexual violence conducted by the Business Coalition for Women (BCFW). The Bank also hosted educational awareness sessions for staff on FSV and the proposed FSV Policy.

***Seated** L-R: Angesula Jogamup, John Nema, Elizabeth Asigau, Naomi Kedea, Aiva Aku, Tommy Minjura.*

***Back** L-R: Olive Imatana, George Geberi, Agnes Mark, Maryanne Kani, Brenda Koan, Ruth Morere-Wapunk, Rosemary Lalaga, Frieda Kamakom, Raylene Semi, Harry Paul and Linsy Pokambut.*

Organisation Chart 31 December 2020



Senior officers 31 December 2020	
Governor	**Loi M. Bakani CMG**
Deputy Governor	Joseph Teria
Secretariat	
Corporate Secretary	Tau Vini
Internal Audit	
Department Manager	Benek Beriso
Manager, Operations Audit	Frieda Kamakom
Manager, IT Audit	Justin Wohuinangu
Financial Analysis and Supervision Unit	
Director	Benny Popoitai MBE
Deputy Director	Wilson Onea
Manager, Supervision & Compliance Division	Rosa Banik
Manager, Intelligence Management Division	Edric Ogomeni
Manager, Policy Development & Coordination Division	Emete Enare
Monetary & Economic Policy Group	
Assistant Governor	Sali David
Economics	
Department Manager	Thomas Jiki
Manager, Monetary Policy and Analysis	Wilson Jonathan
Manager, Balance of Payments	Vacant
Manager, Library	Polycarp Reu
Manager, International Transactions Monitoring	Elim Kiang
Research	
Department Manager	Jeffrey Yabom
Manager, Economic Analysis	Williamina Hubert
Manager, Projects	Boniface Aipi
Financial System Stability Group	
Assistant Governor	Ellison Pidik
Program Manager	
SME Accelerator Program	Dominic Sikakau
Banking Supervision	
Department Manager	Sabina Deklin
Manager, Banks & Finance Companies	Boas Irima
Manager, Savings & Loan Societies	Nickson Kunjil

Senior officers 31 December 2020	
Superannuation & Life Insurance Supervision Department	
Manager	Elizabeth Gima
Manager, Superannuation	Tom Milamala
Manager, Life Insurance	Joseph Nukints
Manager, Employer Contributions Enforcement	Nonza Makip
Financial System Development	
Department Manager	George Awap
Manager, Macro-Prudential Supervision	Mark Ofoi
Manager, Financial System Policy	Tanu Irau
Manager, Licensing and Compliance	Walio Gamini
Finance & Payments Group	
Assistant Governor	Simon Gaius
Payments Oversight & Compliance Office	
Manager	Alfred Napun
Manager, Monitoring & Analytics	Francis Poko
Manager, Assessment & Compliance	Raylene Semi
Financial Markets	
Department Manager	Rowan Rupa
Manager, Foreign Reserves	Seta Kila (Acting)
Manager, Money Markets Operations	Winnie Linken
Manager, Registry	Marie Martin
Manager, Middle Office	Ambrose Papis
Financial Administration	
Department Manager	Danny Ganak
Manager, Management Reporting	Noine Noine
Manager, Accounting & Payments	Pala Tau
Manager, Settlements	Soms Yankey
Banking	
Department Manager	Jason Tirime
Manager, Customer Services	So'on Drewei
Manager, Clearing Accounts	Aiva Aku
Manager, Government Accounts	Priscilla Ipu
Currency	
Department Manager	David Lakatani
Manager, Control	John Yenas
Manager, Processing	Edward Kisaku

Senior officers 31 December 2020	
Payment Systems	
Department Manager	Gaona Gwaibo
Manager, Switch Operations & Support	Stephen Pouru
Corporate Affairs Group	
Assistant Governor	Elizabeth Genia
Strategy & Risk Management Office	
Manager	Nathan Maire
Enterprise Project Management Office	
Manager	Vacant
Human Resources	
Department Manager	Patrick Kwiwa
Manager, Strategy Planning and Development	Mairi Matthew
Manager, Administrative Support	Jennifer Tokome
Manager, Client Support	Vacant
Information & Communication Technology	
Chief Information Officer	Naime Kilamanu
Manager, Corporate Systems	Elvis Haoda
Manager, Operations	Manea Joseph
Corporate Services	
Department Manager	Jerome Peniasi
Manager, Media and E-Communications	Marie Kauna
Manager, General Services	Monica Toisenegila
Manager, Events, Marketing and Publications	Alice Japhlom (Acting)
Facilities & Property Management	
Department Manager	Bruce Kitchen
Manager, Building	Gibson Param
Manager, Security	David Rutana
Currency Processing Facility – Lae	
Manager	Ron Sikar
Manager, Support Services Office	William Tiki
Manager, Cash Processing & Distribution	Frank Ababa
Manager, Cash Control & Distribution	Agnes Mark
Manager, Security	Bravo Vaieke
Manager, Building	Israel Anduari

INFORMATION AND COMMUNICATION TECHNOLOGY

The Information & Communication Technology (ICT) function within the Bank provides oversight, management and delivery of enterprise-wide ICT services.

In 2020 the Bank completed and progressed several strategic projects across the activities of the Bank, including updating and upgrading key systems.

Establish Enterprise Project Management Office (EPMO)

A goal under the ICT Governance Program was to establish the BPNG Enterprise Project Management Office and to acquire project management tools for better portfolio and project management.

The EPMO function was established in the Strategy & Risk Management Office during 2020.

COMMUNICATIONS AND EVENTS COORDINATION

During 2020 the Bank's communications and events staff were involved in a wide range of activities to support the Bank's performance of its key functions and promote public awareness of the role of the central bank.

These included coordinating significant events, including the board meetings, staff farewell and donations to various non-government organisations and groups. As well as major events, the Bank produced and conducted the public release of the two Monetary Policy Statements, issued a range of public information, including the Quarterly Economic Bulletin and Monthly Economic Review and continued public information campaigns.

COMMUNITY SUPPORT

The Bank supports a number of professional, cultural, sporting and health related causes.

2020 was not an appropriate year to participate in anniversary celebrations. The Bank took the decision to cancel celebration activities but instead mark the occasion by donating personal protective equipment and other basic medical supplies to rural hospitals, health centres and clinics. Donations were made to health centres in West New Britain, Milne Bay, Central, Manus, New Ireland, Morobe, Western Highlands and West Sepik provinces and the Autonomous Region of Bougainville.

Deputy Governor Joseph Teria (2nd from left) and Bank staff donated medical supplies to community health posts in Milne Bay Province.

Assistant Governor Ellison Pidik (2nd from left) presented the Bank's donation of medical supplies to a health centre in Manus Province.

BANK OF PAPUA NEW GUINEA

FINANCIAL STATEMENTS
FOR THE YEAR ENDING
31 DECEMBER 2020

Table of contents

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 December 2020

	Notes	2020 K'000	2019 K'000
Revenue from foreign currency investments			
Interest revenue	2	83,073	112,983
Realised gain on financial assets		45,316	23,631
Foreign exchange gains and commissions		69,254	36,637
Total revenue from foreign currency investments		**197,643**	**173,251**
Expenses on foreign currency investments			
Interest expense on liabilities with IMF		(1,411)	(5,204)
Custodian and investment management fees		(6,943)	(6,740)
Total expenses from foreign currency investments		**(8,354)**	**(11,944)**
Net foreign currency income		**189,289**	**161,307**
Revenue from domestic operations			
Interest revenue	3	242,324	275,715
Other income	4	19,471	18,317
Total revenue from domestic operations		**261,795**	**294,032**
Expense on domestic liabilities			
Interest expense	5	(85,502)	(67,214)
Total expenses on domestic liabilities		**(85,502)**	**(67,214)**
Net domestic income		**176,293**	**226,818**
Total net operating income		**365,582**	**388,125**
Operating expenses			
General and administration expenses	6	(234,721)	(231,615)
Profit excluding unrealised income		**130,861**	**156,510**
Other unrealised income			
Fair value and foreign exchange revaluation gain on foreign currency investments		345,299	154,078
Fair value revaluation gain/(loss) on domestic investments		(42,363)	82,780
Profit for the year		**433,797**	**393,368**
Other comprehensive income			
Items that may be subsequently reclassified to Profit or Loss			
Gain on gold asset revaluation		61,583	36,304
Items that will not be subsequently reclassified to Profit or Loss			
Gain on property valuation		-	11,794
Other comprehensive income for the year		**61,583**	**48,098**
Total comprehensive income for the year		**495,380**	**441,466**

The financial statements are to be read in conjunction with the notes on pages 51 to 87.

Statement of Financial Position

For the year ended 31 December 2020

	Notes	2020 K'000	2019 K'000
Assets			
Cash and cash equivalents	8	3,074,377	1,804,862
Financial assets at fair value through profit or loss	9	5,972,573	5,775,555
Assets held with IMF and other financial organisations			
at fair value through profit or loss	7	30,510	30,209
Accrued interest		19,024	19,714
Total foreign currency financial assets		**9,096,484**	**7,630,340**
Government of Papua New Guinea securities	10	1,659,141	2,408,970
Loans and advances	11	1,792	126,093
Accrued interest and other receivables		38,663	58,947
Total local currency financial assets		**1,699,596**	**2,594,010**
Total Financial Assets		**10,796,080**	**10,224,350**
Non-financial assets			
Gold		279,602	218,020
Property and equipment	13	450,497	448,424
Investment properties	14	39,170	39,170
Other assets	12	72,730	68,707
Total non-financial assets		**841,999**	**774,321**
Total Assets		**11,638,079**	**10,998,671**
Liabilities			
Foreign currency financial liabilities			
Liabilities to IMF at fair value through profit or loss	7	640,069	597,335
Other financial liabilities	19	5,697	1,794
Total foreign currency financial liabilities		**645,766**	**599,129**
Local currency financial liabilities			
Deposits from banks and third parties	15	3,619,138	3,625,837
Deposits from Government and Government entities	16	1,623,971	1,351,160
Debt securities issued	17	1,612,924	1,775,731
Accrued interest payable on debt securities		636	2,381
Currency in circulation	18	2,431,093	2,298,574
Other financial liabilities	19	62,877	51,731
Total local currency financial liabilities		**9,350,639**	**9,105,414**
Total financial liabilities		**9,996,405**	**9,704,543**
Non-financial liabilities			
Provisions for employee entitlements	20	35,964	33,798
Total non-financial liabilities		**35,964**	**33,798**
Total Liabilities		**10,032,369**	**9,738,341**

	Notes	2020 K'000	2019 K'000
Equity			
Capital	**22**	145,540	145,540
Gold revaluation reserve	**22**	258,995	197,412
Property revaluation reserve	**22**	95,028	95,028
Unrealised gain/(loss) reserve	**22**	573,890	299,888
Building reserve	**22**	123,800	73,800
General reserve	**22**	30,000	30,000
Retained earnings	**22**	378,457	418,662
Total Equity		**1,605,710**	**1,260,330**
Total Liabilities and Equity		**11,638,079**	**10,998,671**

The financial statements are to be read in conjunction with the notes on pages 51 to 87.

Statement of Changes in Equity

For the year ended 31 December 2020

	Capital K'000	Gold Revaluation Reserve K'000	Property Revaluation Reserve K'000	Unrealised gain (loss) Reserve K'000	Building Reserve K'000	General Reserve K'000	Retained Earnings K'000	Total K'000
Balance at 1 January 2019	**145,540**	**161,108**	**83,234**	**63,030**	**73,800**	**-**	**412,152**	**938,864**
Profit for the year	-	-	-	236,858	-	-	156,510	**393,368**
Net transfers from unrealised profit/(loss) reserve to retained earnings	-	-	-	-	-	-	-	-
Other comprehensive income	-	36,304	-	-	-	-	-	**36,304**
Net transfers from retained earnings to general reserve	-	-	-	-	-	30,000	(30,000)	-
Revaluation of PPE	-	-	11,794	-	-	-	-	**11,794**
Dividend declared and paid	-	-	-	-	-	-	(120,000)	**(120,000)**
Balance at 31 December 2019	**145,540**	**197,412**	**95,028**	**299,888**	**73,800**	**30,000**	**418,662**	**1,260,330**
Profit for the year	-	-	-	302,936	-	-	130,861	**433,797**
Net transfers from unrealised profit/(loss) reserve to retained earnings	-	-	-	(28,934)	-	-	28,934	-
Other comprehensive income	-	61,583	-	-	-	-	-	**61,583**
Net transfers from retained earnings to building reserve	-	-	-	-	50,000	-	(50,000)	-
Revaluation of PPE	-	-	-	-	-	-	-	-
Dividend declared and paid	-	-	-	-	-	-	(150,000)	**(150,000)**
Balance at 31 December 2020	**145,540**	**258,995**	**95,028**	**573,890**	**123,800**	**30,000**	**378,457**	**1,605,710**

The realised profit for the year is K130.8 million. The unrealised gain/(loss) reserve and net asset balance at 31 December 2020 are K573.9 million and K1.6 billion, respectively. The *Central Banking Act 2000* states that no distribution will be made where, in the opinion of the Central Bank, the assets of the Bank are, or after the payment would be, less than the sum of its liabilities and paid-up capital.

The financial statements are to be read in conjunction with the notes on pages 51 to 87.

Statement of Cash Flows

For the year ended 31 December 2020

	Notes	2020 K'000	2019 K'000
Cash Flows from Operating Activities			
Interest received on foreign investments		83,763	112,731
Interest received on domestic investments		262,609	280,203
Fees, commissions and other income received		88,725	54,954
Interest paid on IMF liabilities		(1,411)	(1,604)
Interest paid on domestic liabilities		(87,247)	(66,584)
Payments to employees		(103,303)	(89,946)
Payments to suppliers		(90,748)	(113,797)
Fees and commissions paid		(6,943)	(6,740)
Net proceeds from sale of foreign investments		236,031	(26,419)
Net receipts from Government Securities		707,466	337,068
Net loans repaid/(issued)		124,301	22,933
Net Cash Flow (used in)/provided by Operating Activities		**1,213,243**	**502,799**
Cash Flows from Investing Activities			
Purchase of property and equipment		(8,877)	(47,468)
Payments for construction costs on capital projects		(20,698)	(45,047)
Proceeds from sale of property and equipment		23	44
Net Cash Flow used in Investing Activities		**(29,552)**	**(92,471)**
Cash Flows from Financing Activities			
Net movement of currency in circulation		132,519	146,580
Net movement in debt securities issued		(162,807)	(626,923)
Distributions to the Government		(150,000)	(120,000)
Net movement in deposits from Government		272,811	(154,263)
Net movement in deposits from banks		(6,699)	509,103
Net Cash Flow provided/(used in) by Financing Activities		**85,824**	**(245,503)**
Net Increase in Cash and Cash Equivalents		**1,269,515**	**164,825**
Cash and cash equivalents at 1 January		1,804,862	1,640,037
Cash and Cash Equivalents at 31 December	8	**3,074,377**	**1,804,862**

The financial statements are to be read in conjunction with the notes on pages 51 to 87.

Notes to the Financial Statements

For the year ended
31 December 2020

Note 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Bank of Papua New Guinea (the 'Bank') is domiciled in Papua New Guinea and is the country's central bank and regulator of monetary policy, the financial sector and payments system.

The principal accounting policies applied in the preparation of these financial statements are set out below. The application of these policies are consistent with the review and approval from the Bank's Board as at 30 June 2021.

(a) Basis of preparation

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), and in accordance with the *Central Banking Act 2000* (the "Act"). In the event of any conflict between the requirements of the Act and the Accounting Standards, the Bank is required to comply with the Act.

All amounts are expressed in kina rounded to the nearest thousand unless otherwise stated. Fair value accounting is used for all the Bank's major assets, including domestic and foreign marketable securities, gold and foreign currency, as well as for land and buildings. In all other cases, a historical cost basis of accounting is used. Revenues and expenses are brought to account on an accrual basis.

Going concern

The financial statements continue to be prepared on a going concern basis. The Bank recorded a net asset position of K1.61 billion as at 31 December 2020 (2019: net asset of K1.26 billion). This steady improvement in the Bank's net asset position over the last five years is mainly driven by continued depreciation of the kina, which is giving rise to the value of foreign assets.

Section 50(2) of the Act provides that where the Bank incurs a loss due to a change in the value of assets or liabilities, the Minister shall cause to be paid to the Bank such amount out of the Consolidated Revenue Fund as is necessary to avoid the loss. Subsection 50(4) of that Act further provides that the Minister may create and issue to the Central Bank non-interest bearing non-negotiable notes for an amount not exceeding any payment made by the Minister to the Central Bank out of the Consolidated Revenue Fund in accordance with Subsections (1) and (2) of the Act. The above provisions of the Act effectively require the Government to provide financial support to the Bank.

(b) Functional and presentation currency

Transactions in foreign currency are translated to kina being the functional and presentation currency of the Bank at the foreign exchange rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to kina at the foreign exchange rate prevailing at reporting date. Foreign exchange differences arising on translation are recognised in the Statement of Profit or Loss and Other comprehensive income.

(c) Use of judgements and estimates

In preparing these financial statements, management has made judgements, estimates and assumptions that affect the application of the Bank's accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

(i) Assumptions and estimation uncertainties

Information about assumptions and estimation uncertainties that have a significant risk resulting in a material adjustment in the year ended 31 December 2020 is set out below in relation to the impairment of financial instruments and in the following notes in relation to other areas:

Note 24 (iv) – determination of the fair value of financial instruments with significant unobservable inputs;

Note 14 – fair value of investment properties; and

Note 13 – fair value of land and buildings.

(ii) Accounting estimates

Fair value of financial instruments that are not traded in an active market (for example over the counter derivatives or PNG Government inscribed stock) is determined using valuation techniques. The Bank uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period. Derivative transactions are entered into on behalf of the Bank by the external fund managers and similar valuation techniques are used in valuing these derivatives.

These financial statements are not considered to contain any significant accounting estimates, as the most significant balance sheet items can be valued with reference to market rates, and revenue and expense recognition criteria are clearly defined.

(d) Standards issued but not adopted

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2020 and earlier application is permitted; however, the Bank has not early adopted them in preparing financial statements. The following amended standards are not expected to have a significant impact on the Bank's financial statements.

- References to Conceptual Framework in IFRS Standards (Amendments to IFRS 3)
- Definition of a Business (Amendments to IFRS 3).
- IFRS 17 Insurance Contracts and amendments to IFRS 17 Insurance Contracts
- Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37)
- COVID-19 Related Rent Concessions (Amendments to IFRS 16)
- Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16)
- Classification of Liabilities as Current or Non-current (Amendments to IAS 1)

(e) IFRS 16 Leases

This standard was effective for the Bank's annual reporting period beginning on 1 January 2019. IFRS 16 requires a lessee to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments. Under the standard, the Bank will reflect in the Statement of Financial Position the right-of-use assets and lease liabilities in respect of the lease agreements. The impact on the Statement of Financial Position and the Statement of Comprehensive Income is being assessed by the Bank.

(i) The Bank as lessee

The Bank assesses whether a contract is, or contains a lease, at inception of the contract. The Bank recognises a right-of-use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less or residential leases) and leases of low value assets (such as tablets and personal computers, small items of office furniture and telephones). For these leases, the Bank recognises the lease payments as an operating expense on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern in which economic benefits from the leased assets are consumed.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted by using the rate implicit in the lease. If this rate cannot be readily determined, the Bank uses its Kina Facility Rate.

Lease payments included in the measurement of the lease liability comprise:

- Fixed lease payments (including in-substance fixed payments), less any lease incentives receivable;
- Variable lease payments that depend on an index or rate, initially measured using the index or rate at the commencement date;
- The amount expected to be payable by the lessee under residual value guarantees;
- The exercise price of purchase options, if the lessee is reasonably certain to exercise the options; and
- Payments of penalties for terminating the lease, if the lease term reflects the exercise of an option to terminate the lease.

The lease liability is included under 'Other financial liabilities' in the statement of financial position.

The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability (using the effective interest method) and by reducing the carrying amount to reflect the lease payments made.

The Bank remeasures the lease liability (and makes a corresponding adjustment to the related right-of-use asset) whenever:

- The lease term has changed or there is a significant event or change in circumstances resulting in a change in the assessment of exercise of a purchase option, in which case the lease liability is remeasured by discounting the revised lease payments using the current Kina Facility Rate.
- The lease payments change due to changes in an index or rate or a change in expected payment under a guaranteed residual value, in which cases the lease liability is remeasured by discounting the revised lease payments using an unchanged discount rate (unless the lease payments change is due to a change in a floating interest rate, in which case a revised discount rate is used).
- A lease contract is modified and the lease modification is not accounted for as a separate lease, in which case the lease liability is remeasured based on the lease term of the modified lease by discounting the revised lease payments using a revised discount rate at the effective date of the modification.

The Bank did not make any such adjustments during the periods presented.

The right-of-use assets comprise the initial measurement of the corresponding lease liability, lease payments made at or before the commencement day, less any lease incentives received and any initial direct costs. They are subsequently measured at cost less accumulated depreciation and impairment losses.

Whenever the Bank incurs an obligation for costs to dismantle and remove a leased asset, restore the site on which it is located or restore the underlying asset to the condition required by the terms and conditions of the lease, a provision is recognised and measured under IAS 37. To the extent that the costs relate to a right-of-use asset, the costs are included in the related right-of-use asset, unless those costs are incurred to produce inventories.

Right-of-use assets are depreciated over the shorter period of lease term and useful life of the underlying asset. If a lease transfers ownership of the underlying asset or the cost of the right-of-use asset reflects that the Bank expects to exercise a purchase option, the related right-of-use asset is depreciated over the useful life of the underlying asset. The depreciation starts at the commencement date of the lease.

The right-of-use assets are included in the Property and equipment line in the Statements of Financial Position.

The Bank applies IAS 36 to determine whether a right-of-use asset is impaired and accounts for any identified impairment loss as described in note 21.

Variable rents that do not depend on an index or rate are not included in the measurement of the lease liability and the right-of-use asset. The related payments are recognised as an expense in the period in which the event or condition that triggers those payments occurs and are included in the line Other expenses in Profit or Loss.

(ii) The Bank as lessor

The Bank enters into lease agreements as a lessor with respect to its investment properties.

Leases for which the Bank is a lessor are classified as finance or operating leases. Whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee, the contract is classified as a finance lease. All other leases are classified as operating leases.

When the Bank is an intermediate lessor, it accounts for the head lease and the sub-lease as two separate contracts. The sub-lease is classified as a finance or operating lease by reference to the right-of-use asset arising from the head lease.

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term.

Amounts due from lessees under finance leases are recognised as receivables at the amount of the Bank's net investment in the leases.

(f) Financial Instruments

Classification and measurement of financial instruments

Definition of financial instruments

A financial instrument is defined as any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity. The Bank's financial instruments are its domestic government securities, foreign government securities, Central Bank Bills issued, bank deposits, cash and cash equivalents, deposit liabilities and currency in circulation. The Bank accounts for its financial instruments in accordance with IFRS 9 and reports these instruments under IFRS 7 Financial Instruments: Disclosures and IFRS 13 Fair Value Measurement.

(i) Recognition and initial measurement

Financial instruments are initially recognised when an entity becomes a party to the contractual provisions of the instrument, and are classified into various categories depending upon the type of instrument, which then determines the subsequent measurement of the instrument.

(ii) Classification and subsequent measurement of financial assets

The Bank classifies financial assets into one of the following measurement categories:

- Amortised cost;
- Fair value through other comprehensive income (FVTOCI); or
- Fair value through profit or loss (FVTPL).

The classification of debt instruments is determined based on:

a) the business model under which the asset is held; and

b) the contractual cash flow characteristics of the instrument.

Business model assessment

Business model assessment involves determining how financial assets are managed in order to generate cash flows. The business model for debt instruments is to hold assets and collect contractual cash flows. Any sales of the asset are incidental to the objective of the model. The contractual cash flow characteristics assessment involves assessing the contractual features of an instrument to determine if they give rise to cash flows that are consistent with a basic lending arrangement. Contractual cash flows are consistent with a basic lending arrangement if they represent cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI). Principal is defined as the fair value of the instrument at initial recognition. Principal may change over the life of the instrument due to repayments or amortisation of premium/discount. Interest is defined as the consideration for the time value of money and the credit risk associated with the principal amount outstanding and for other basic lending risks and costs, and a profit margin. If the Bank identifies any contractual features that could significantly modify the cash flows of the instrument such that they are no longer consistent with a basic lending arrangement, the related financial asset is classified and measured at FVTPL.

Solely payments of principle and interest (SPPI) criteria

The SPPI test requires that the contractual terms of the financial asset (as a whole) give rise to cash flows that are solely payments of principal and interest on the principal amounts outstanding i.e. cash flows that are consistent with a basic lending arrangement.

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money — e.g. periodical reset of interest rates.

Financial assets measured at amortised cost – financial assets are measured at amortised cost if they are held within a business model whose objective is to hold for collection of contractual cash flows, where those cash flows represent solely payments of principal and interest. After initial measurement, financial assets in this category are carried at amortised cost. Interest income on these instruments is recognised as interest income using the effective interest rate method.

Financial assets measured at FVTPL – financial assets are measured at FVTPL if assets:

i) are held for trading purposes;

ii) are held as part of a portfolio managed on a fair value basis; or

iii) whose cash flows do not represent payments that are solely payments of principal and interest.

Financial assets measured at FVTOCI – financial assets are measured at FVTOCI if the financial assets are held within a business model that is achieved by both collecting contractual cash flows and selling, which contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest. These comprise primarily marketable securities. They are recognised at the trade date when the Bank enters into contractual arrangements to purchase and are derecognised when they are sold or redeemed. They are subsequently remeasured at fair value and changes therein (except for those relating to impairment, interest income and foreign currency exchange gains or losses) are recognised in other comprehensive income until the assets are sold. Upon disposal, the cumulative gains and losses in the comprehensive income are recognised in the income statement as 'gains and losses from financial instruments'. Financial assets measured at FVOCI are included in the impairment calculations and the impairment is recognised in profit or loss.

(iii) Classification of financial liabilities

The Bank classifies all financial liabilities as subsequently measured at amortised cost except for liabilities with IMF. Interest on financial liabilities is calculated using the effective interest rate method and is recognised as interest expense. Financial liabilities measured at fair value through profit or loss – the Bank designates financial liabilities to eliminate, or significantly reduce, inconsistencies that would otherwise arise from measuring assets and liabilities on different bases. The relevant assets and liabilities (including derivatives) are managed together and internal reporting is evaluated on a fair value basis.

(iv) Reclassifications of financial assets

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing the financial assets.

(v) Impairment of financial assets carried at amortised cost

The Bank applies a three-stage approach to measure allowance for credit losses, using an expected credit loss approach as required under IFRS 9.

Expected credit loss impairment model

The Bank's allowance for credit losses calculations are outputs of models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. The expected credit loss impairment model reflects the present value of all cash shortfalls related to default events either (i) over the following twelve months or (ii) over the expected life of a financial instrument depending on credit deterioration from inception. The allowance for credit losses reflects an unbiased, probability-weighted outcome which considers multiple scenarios based on reasonable and supportable forecasts.

This impairment model measures credit loss allowances using a three-stage approach based on the extent of credit deterioration since origination:

- **Stage 1 –** 12-month ECL applies to all financial assets that have not experienced a significant increase in credit risk (SICR) since origination and are not credit impaired. The ECL will be computed using a 12-month probability of default that represents the probability of default occurring over the next 12 months. For those assets with a remaining maturity of less than 12 months, a PD is used that corresponds to remaining maturity.
- **Stage 2 –** When a financial asset experiences a SICR subsequent to origination but is not credit impaired, it is considered to be in Stage 2. This requires the computation of ECL based on lifetime probability of default that represents the probability of default occurring over the remaining estimated life of the financial asset. Credit loss allowances are higher in this stage because of an increase in risk and the impact of a longer time horizon being considered compared to 12 months in Stage 1. When determining whether the credit risk (i.e. risk of default) on a financial instrument has increased significantly since initial recognition, the Bank will consider reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information and analysis based on the Bank's historical experience, expert credit assessment and forward looking information.
- **Stage 3 –** Financial assets that have an objective evidence of impairment will be included in this stage. Similar to Stage 2, the allowance for credit losses will continue to capture the lifetime expected credit losses. Under IFRS 9, the Bank will consider a financial asset to be in default when the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held).

Measurement of expected credit loss

The probability of default (PD), exposure at default (EAD), and loss given default (LGD) inputs used to estimate expected credit losses are modelled based on macroeconomic variables that are most closely related with credit losses in the relevant portfolio. Details of key statistical parameters/inputs are as follows:

- PD – The probability of default is an estimate of the likelihood of default over a given time horizon.

A default may only happen at a certain time over the remaining estimated life, if the facility has not been previously derecognised and is still in the portfolio.

- EAD – The exposure at default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.

- LGD – The loss given default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the Company would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

Forward-looking information

The Bank formulates a base case view of the future direction of relevant economic variables and a representative range of other possible forecast scenarios and consideration of a variety of external actual and forecast information. This process involves developing four different economic scenarios, which represent a range of scenarios linked to housing and interest rate variables. The Bank has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments, choosing scenarios that specifically test the resilience of the Bank to financial stress.

ECL calculation

Expected credit losses are calculated by identifying scenarios in which a loan or receivable defaults, estimating the cash shortfall that would be incurred and then multiplying that loss by the probability of the default happening. When an ECL is identified, the carrying amount of the asset would be reduced and the amount of ECL is recognised in the income statement.

(vi) Derecognition of financial instruments

Derecognition of financial assets

A financial asset is derecognised when the contractual rights to the cash flows from the asset has expired; or the Bank transfers the contractual rights to receive the cash flows from the financial asset; or has assumed an obligation to pay those cash flows to an independent third-party; or the Bank has transferred substantially all the risks and rewards of ownership of that asset to an independent third-party. Management determines whether substantially all the risk and rewards of ownership have been transferred by quantitatively comparing the variability in cash flows before and after the transfer. If the variability in cash flows remains significantly similar subsequent to the transfer, the Bank has retained substantially all of the risks and rewards of ownership.

Where substantially all the risks and rewards of ownership of the financial asset are neither retained nor transferred, the Bank derecognises the transferred asset only if it has lost control over that asset. Control over the asset is represented by the practical ability to sell the transferred asset. If the Bank retains control over the asset, it will continue to recognise the asset to the extent of its continuing involvement. At times such continuing involvement may be in the form of investment in senior or subordinated tranches of notes issued by non-consolidated structured entities.

On derecognition of a financial asset, the difference between the carrying amount and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in Other comprehensive income is recognised in the Profit or Loss.

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expires. If an existing financial liability is replaced by another from the same counterparty on substantially different terms, or the terms of the existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability at fair value.

The difference in the respective carrying amount of the existing liability and the new liability is recognised as a gain/loss in the Profit or Loss.

(vii) Modification of financial instruments

Modification of financial assets

If the terms of a financial asset are modified, then the Bank evaluates whether the cash flows of the modified asset are substantially different.

If the cash flows are substantially different, then the contractual rights to cash flows from the original assets are deemed to have expired. In this case, the original financial asset is derecognised and a new financial asset is recognised at fair value plus any eligible transaction costs.

If the modification of a financial asset measured at amortised cost or FVTOCI does not result in derecognition of the financial asset, then the Bank first recalculates the gross carrying amount of the financial asset using the effective interest rate of the asset and recognises the resulting adjustment as a modification gain or loss in Profit or Loss.

Modification of financial liabilities

The Bank derecognises a financial liability when its terms are modified and cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and the consideration paid is recognised in Profit or Loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

(viii) Domestic Government securities

The Bank holds Inscribed stocks with fixed coupon rates issued by the Government. Interest is received biannually at the coupon rate and the principal is received at maturity. The Inscribed stock securities are managed by the Bank on a fair value basis, and are held to implement monetary policy and may be sold or lent, typically for short terms, under repurchase agreements, thus they are designated as FVTPL under IFRS 9. In accordance with this standard, the securities are accounted for on a fair value basis using the discounted present value model, with realised and unrealised gains and losses taken to profit. The Bank also holds Treasury bills purchased at a discount. The securities are held to collect contractual cash flows, hence are measured at amortised cost.

Interest earned on the securities is accrued over the term of the security and included as revenue in the Statement of Profit or Loss and Other comprehensive income.

(ix) Foreign exchange holdings

Foreign exchange holdings are invested mainly in securities (issued by the Governments of Australia, the United Kingdom, United States of America, Germany, France and Japan) and bank deposits (with highly-rated international banks, central banks and international agencies). They are available to be traded in managing the portfolio of foreign exchange reserves. In accordance with IFRS 9, these assets are measured as 'fair value through profit or loss'. External fund managers engaged by the Bank also enter into forward exchange contracts to hedge the returns of portfolios under their management to the US Dollar. No PNG kina forward contracts are entered into.

(x) Foreign exchange translation

Assets and liabilities denominated in foreign currency are converted to kina equivalents at the prevailing exchange rate on balance date in accordance with IAS 21 – The Effects of Changes in Foreign Exchange Rates. Realised and unrealised gains or losses on foreign currency are taken to Profit or Loss, but only realised gains are available for distribution.

(xi) Foreign government securities

Foreign government securities include coupon and discounted securities. Coupon securities have biannual or annual interest payments depending on the currency and type of security; the principal is received at maturity. Interest earned on discount securities is the difference between the purchase cost and the face value of the security; this is accrued over the term the securities are held. They are available to be traded in managing the portfolio of foreign exchange reserves and are managed by the Bank on a fair value basis, thus they are measured as FVTPL under IFRS 9. In accordance with this standard, these securities are valued at market bid prices on balance date. Realised and unrealised gains or losses are taken to Profit; only realised gains and losses are available for distribution in accordance with the *Central Banking Act 2000*. Interest earned on securities is accrued as revenue in the Statement of Profit or Loss and Other Comprehensive Income.

(xii) Foreign deposits

The Bank holds its foreign currency reserves in deposits with highly-rated international banks. Deposits are classified as Cash and cash equivalents under IAS 7 and recorded at their face value. Foreign deposits are revalued at period end using the applicable foreign exchange bid rate. Any gains or losses due to changes in the foreign exchange rates between periods are taken to profit.

(xiii) Foreign currency forward contracts

External fund managers engaged to manage part of the Bank's investment portfolio enter into over-the-counter forward foreign exchange contracts to hedge the return of portfolios under their management to the US dollar. Gains/(losses) on this portfolio are treated as unrealised by the Bank and recorded in a separate equity reserve as such gains and losses are not available for distribution. These forward contracts are accounted for on a fair value basis, with all changes in fair value being reflected in the Statement of Profit or Loss and Other comprehensive income in accordance with IFRS 9. The fair values are determined with reference to prevailing exchange rates at balance date.

(xiv) Repurchase agreements

A repurchase agreement involves the sale of securities with an undertaking to repurchase them on an agreed future date at an agreed price. In a reverse repurchase agreement, securities are initially bought and this transaction is reversed at an agreed price on an agreed future date. Reverse repurchase agreements provide the Bank's counterparties with cash for the term of the agreement and the Bank treats it as a cash receivable. Securities purchased and contracted for sale under reverse repurchase agreements are classified under IFRS 9 as 'held to collect' and measured at amortised cost. The difference between the purchase and sale price is accrued over the term of the agreement and recognised as interest revenue. Repurchase agreements result in cash being paid to the Bank and are treated as a liability, reflecting the obligation to repay cash.

(xv) Deposit liabilities

Deposits include deposits at call. Deposits are financial liabilities classified and measured at amortised cost under IFRS 9 and are included in Note 15.

(xvi) Central Bank Bills on issue

The Bank has issued Central Bank Bills as part of its money market operations. These are classified as financial liabilities. The Bills issued have maturities ranging from 28 days to 181 days and are recorded at their amortised cost using the effective interest method. Interest is paid at maturity.

The Bank is also issuing Central Bank bond with maturities ranging from 2 to 10 years and are also recorded at amortised cost using the effective interest method. Interest is paid semi-annually.

(xvii) Loans and Advances

Loans and advances are non-derivative financial assets with fixed or determinable repayment terms that are not quoted in an active market. Loans are receivables and initially recognised at fair value which is the cash consideration to originate or purchase the loan including any transaction costs and measured subsequently at amortised cost using the effective interest rate method under IFRS 9. Loans and advances owing from previous staff are treated as financial assets measured at amortised cost and will be assessed for impairment based on an expected credit loss model in accordance with IFRS 9; however, loans and advances to current staff represent a prepaid employee benefit (a non-financial asset).

(xviii) Assets and Liabilities with the International Monetary Fund (IMF)

As Papua New Guinea is an IMF member nation, special drawing rights (SDR) are periodically allocated. The Bank recognises the holdings as an asset and allocation as a liability. The IMF assets and liabilities are denominated in SDR which are based on the weighted average of five main trading currencies. These are translated to PGK using the SDR market rate at balance date. Under voluntary arrangements with the IMF, the Bank is willing to transact in SDRs upon request from other countries or prescribed holders. In these transactions, the Bank will generally either buy or sell SDRs in exchange for foreign currencies. These assets and liabilities are managed by the Bank on a fair value basis and are measured as FVTPL in accordance with IFRS 9.

(xix) Currency in Circulation

Currency issued by the Bank represents a claim on the Bank in favour of the holder. It is recorded at face value in the Statement of Financial Position.

(xx) Revenue

Interest income

Interest income is recognised as it accrues in the Statement of Profit or Loss and Other Comprehensive Income using the effective interest rate ("EIR") method in line with requirements of IFRS 9.

Foreign exchange gains and commissions

Foreign exchange gains and commissions include gains and losses on trading in foreign currency and profit or loss impact of conversion to functional currency of foreign currency denominated assets and liabilities.

Realised gains/(loss) on financial assets

Gains and losses realised from the sale of foreign financial instruments are reflected in the Statement of Profit or Loss and Other Comprehensive Income at the time of transaction.

Other income

Rental income is brought to account as the performance obligations are satisfied over time. All rents are payable on a monthly basis. All other income sources are generally brought to account as the performance obligations are satisfied at a point in time, with the exception of license and application fees which are brought to account over time.

(g) Determination of fair value

For financial instruments trading in active markets, the determination of fair values of financial assets and financial liabilities is based on quoted market prices. This includes quoted debt instruments on major trading exchanges and broker quotes from Bloomberg and Reuters.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from the exchange, dealer, broker, pricing service or regulatory agencies, and those prices represent actual and regularly occurring market transactions on an arm's length basis.

For all other financial instruments, fair value is determined using valuation techniques. In these techniques, fair values are estimated from observable data in respect of similar financial instruments, using models to estimate the present value of expected future cash flows or other valuation techniques, using inputs (for example, foreign exchange rates, volatilities and counterparty spreads) existing at the dates of the statement of financial position.

For more complex instruments, the Bank uses internally developed models, which are usually based on valuation methods and techniques generally recognised as standard within the industry. Valuation models are used primarily to value unlisted debt securities and other debt instruments for which markets were or have become illiquid. Some of the inputs to these models may not be market observable and are therefore estimated based on assumptions.

(h) Property and equipment

Formal valuations of all the Bank's properties are conducted on a triennial basis. The properties are valued by local independent valuers. The most recent independent desktop valuation of the properties was conducted in the financial statements at 31 December 2020. In accordance with IAS 16 – Property Plant and Equipment, properties are valued at fair value, which reflects observable prices and are based on the assumption that assets would be exchanged between knowledgeable, willing parties at arm's length. Reflecting their specialised nature, the Bank's head office at ToRobert Haus and the Lae Currency Processing Facility are valued at depreciated replacement cost. Valuation gains and losses are transferred to the Property Revaluation Reserve. Management has assessed the fair value of all property and equipment as at year end and consider them to be appropriate. Property Revaluations are done and accounted for at the end of the year applying the elimination method to any accumulated depreciation.

Annual depreciation is based on fair values less their estimated residual values using the straight-line method over their estimated useful lives, and is recognised in the profit or loss. The range of useful lives used for each class of assets is:

	Years
Residential Properties	20 – 30
Office Buildings	50
Computer Equipment	5
Vehicles	4
Equipment	5
Intangible – Computer Software Licenses	13

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

(i) Computer software

Computer software that is internally developed or purchased is accounted for in accordance with IAS 38 – Intangible Assets. Intangibles are recognised at cost less accumulated amortisation and impairment adjustments (if any), details of which are included in Note 13.

Amortisation of computer software is calculated on a straight-line basis using the estimate useful life of the relevant asset which is usually a period of between three to five years. The useful life of core banking software may be up to 13 years, reflecting the period over which the future economic benefits are expected to be realised from this asset.

(j) Gold

Gold reserves placed on deposit with a financial institution are valued at the kina equivalent of the prevailing exchange rate at balance date. On this basis, the underlying transaction means that the Bank holds a gold asset which is separately disclosed as gold. Unrealised gains and losses on gold are transferred to Other comprehensive income.

(k) Investment properties

Investment property is initially measured at cost and subsequently at fair value, with any change therein recognised in Profit or Loss within Other unrealised income: Fair value revaluation gain on domestic investment.

When the use of a Property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting. Any gain or loss on disposal of investment property (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in Profit or Loss.

(l) Investment property rental income

Rental income from investment property is recognised in Other income from domestic investments on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

(m) Derecognition

A financial asset is derecognised when the rights to receive cash flows from the financial asset have expired. The Bank also derecognises the financial asset if it has both transferred the financial asset and the transfer qualifies for derecognition under IFRS 9. A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expires.

(n) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the Statement of Financial Position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

(o) Inventory – notes and coins

The cost of the printing of notes and minting of coins are initially capitalised until such time as they are issued into circulation at which point the related cost is expensed. The weighted average cost method is used to calculate the number of pieces issued into circulation. All other expenditures of a non-capital nature are expensed when incurred.

(p) Cash and cash equivalents

Cash and cash equivalents comprise balances with a maturity of less than three months from the date of acquisition, including cash on hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less.

(q) Other receivables

Other receivables are stated at amortised cost.

(r) Employee benefits

(i) Pension fund

The Governor and Deputy Governor contribute to the Bank's defined benefit pension fund and all other employees contribute to an approved external superannuation fund. Interest is paid on the Bank's pension fund balance half yearly based on the average interest rate of Nasfund and Nambawan Superannuation Fund.

Contributions to the Bank's pension fund and external superannuation fund are recognised as an expense in the Bank's Statement of Profit or Loss and Other comprehensive income. The value of the Bank's pension fund defined benefit obligations and the fair value of the Bank's pension fund assets are determined with sufficient regularity to ensure that the amounts recognised in the Bank's financial statements do not differ materially from the amounts that would be determined at the balance date.

(ii) Provision for leave entitlement

The Bank maintains provisions for accrued annual leave in accordance with IAS 19 - Employees Benefits, calculated on salaries expected to prevail when leave is anticipated to be taken. The Bank also maintains provisions for long service leave. The provision of employee benefits for long service leave represent the present value of the estimated future cash outflows to be made resulting from employees' service provided to balance date. The provision is calculated using expected future increases in wages and salary rates including related on-costs and expected settlement dates based on staff turnover history and is discounted using the rates attaching to PNG Government bonds at balance date which most closely match the terms of maturity of the related liabilities.

(s) Other liabilities

Other liabilities are initially recognised at their fair value and subsequently recognised at amortised cost.

(t) Reserves

The Bank maintains the following reserves. Their purpose and method of operation is to be as follows:

(i) Bank of Papua New Guinea Reserve Fund

The *Central Banking Act 2000* Section 42, allows the Bank to create reserve funds for meeting contingencies which arise in the course of operations in carrying out its functions. The bank currently has a General Reserve and Building Reserve fund.

(ii) Property Revaluation Reserve

The property revaluation reserve reflects the impact of changes in the fair value of property.

(iii) Unrealised Profits Reserve

Unrealised gains and losses on foreign exchange balances and domestic securities are recognised in the unrealised loss reserve until such gains and losses are realised whereby they are recognised in Profit and Loss from ordinary activities. Such gains and losses are not available for distribution.

(iv) Distributable Profit Reserve

The distributable profit reserve reflects closing distributable profit which may be distributed to the Government of Papua New Guinea after ensuring that the current financial position of the Bank meets the requirements under the *Central Banking Act 2000* Section 49(3).

(v) Gold Revaluation Reserve

Unrealised gains and losses arising from revaluation are recognised in the Gold Revaluation Reserve at end of the accounting period. Realised gains and losses are recognised in Profit and Loss from ordinary activities.

(u) Determination of distributable profit

Profits of the Bank are determined and dealt with in accordance with Sections 49 and 50 of the *Central Banking Act 2000* as follows:

(i) Section 50 (1) states that net profit arising from revaluation and foreign currency movements shall not be available to be distributed to the Government or paid into the Consolidated Revenue Fund. Accordingly such unrealised profits are transferred to the Unrealised Profits Reserve.

(ii) The Board of the Bank is required to determine the net profit of the Bank and then consult with the Minister for Treasury to determine the amount of profit that is to be placed to the credit of the Bank's reserves.

(iii) The balance of net profit after any transfer in (a) and (b) in accordance with Sections 49(2)(a) and 50(1) of the Act is paid to the Consolidated Revenue Fund.

(iv) The amount shall not be paid into the Consolidated Revenue Fund under the above sections where, in the opinion of the Central Bank, the assets of the Central Bank are, or after the payment would be, less than the sum of its liabilities and paid-up capital.

(v) The unrealised profit reserve of the Bank represents gains or loss arising from the revaluation of gold, properties and other financial assets of the Bank. These gains and losses are separately classified under the respective reserves in the Statement of Changes in Equity.

(v) Tax Exemption

Bank of Papua New Guinea is exempt from income tax under section 87 of the *Central Banking Act 2000*.

(w) Comparatives

Comparative financial information has been reclassified to conform to current year presentation where necessary.

(x) Rounding

Financial information has been rounded to the nearest thousand kina.

	2020 K'000	2019 K'000
Note 2: INTEREST REVENUE – FOREIGN CURRENCY INVESTMENTS		
Foreign securities and bank deposits	83,073	112,983
	83,073	**112,983**

Interest income on foreign investments includes interest earned on foreign bonds, Treasury bills, nostro accounts and other foreign investments. Income of K60.0 million (2019: K63.8 million) is in relation to investments managed by external fund managers and the remainder of K23.0 million (2019: K49.2 million) relates to investments managed by the Bank. Coupon rates during the year varied between 0.8% and 1.0% (2019: 0.0% and 1.8%) and yields varied between 0.0% and 0.4% (2019: 0% and 1.5%). Interest is recognised on an effective interest rate basis.

Note 3: INTEREST REVENUE – DOMESTIC OPERATIONS

	2020 K'000	2019 K'000
Inscribed stock and other Government securities	230,388	267,465
Temporary advances to Government	11,189	4,245
Overnight lending to commercial banks	747	4,005
	242,324	**275,715**

Interest income earned on Government Inscribed stock amounted to K207.3 million (2019: K238.2 million) while K33.9 million was earned from Government Treasury bills (2019: K28.9 million). During the year coupon rates on Inscribed stock varied between 8% and 12.5% (2019: 8% and 14%) while yields on Treasury bills varied between 4.7% and 7.2% (2019: 4.7% and 8.1%). Interest is recognised on an effective interest rate basis.

Note 4: OTHER INCOME – DOMESTIC OPERATIONS

	2020 K'000	2019 K'000
Licensing and other fees	13,814	12,675
Numismatic currency	163	246
Property rent	5,085	4,673
Other	409	723
	19,471	**18,317**

Note 5: INTEREST EXPENSE – DOMESTIC OPERATIONS

	2020 K'000	2019 K'000
Central Bank Bills issued	84,538	66,041
Other deposits held	281	291
Lease interest expense	683	882
	85,502	**67,214**

Interest on securities issued varied between 1.4% and 12.03% during the year (2019: 1.4% and 11.98%). Interest is recognised on an effective interest rate basis.

	2020 K'000	2019 K'000
Note 6: GENERAL AND ADMINISTRATION EXPENSES		
Staff costs	105,469	87,602
Premises and equipment	43,265	56,642
Other expenses	26,631	18,008
Depreciation of property and equipment	27,479	22,040
Travel	6,139	13,125
Amortisation of notes and coins production expenses	13,130	15,122
Legal and consultancy fees	6,487	6,873
Staff training and development	2,252	6,475
Board and meeting expenses	1,256	1,873
Currency distribution expenses	1,140	1,947
Audit fee	1,473	1,908
	234,721	**231,615**

Note 7: IMF AND OTHER FINANCIAL ORGANISATION RELATED ASSETS & LIABILITIES

	2020 K'000	2019 K'000
Assets – mandatorily measured at FVTPL		
IMF SDR holdings and deposits and other Organisations	30,510	30,209
	30,510	**30,209**
Liabilities – designated as FVTPL		
IMF number 1 and 2 loan accounts	5,939	5,939
SDR allocation	634,130	591,396
	640,069	**597,335**

Papua New Guinea has been a member of the IMF since 1975. The Bank of Papua New Guinea acts as the fiscal agent for the IMF on behalf of the Government. As fiscal agent, the Bank of Papua New Guinea is authorised to carry out all operations and transactions with the Fund.

Special Drawing Rights (SDR) are allocated by the IMF to members on the basis of members' quota at the time of the SDR allocation. The Bank of Papua New Guinea pays interest on its SDR allocations and earns interest on its holdings of SDR.

Note 8: CASH & CASH EQUIVALENTS

	2020 K'000	2019 K'000
Foreign currency holdings - Nostro accounts	3,074,377	1,804,862
	3,074,377	**1,804,862**

The nostro accounts represent the Bank's foreign currency holdings with corresponding foreign banks.

	2020 K'000	2019 K'000

Note 9: FINANCIAL ASSETS AT FAIR VALUE

	2020 K'000	2019 K'000
Foreign investments – mandatorily measured at FVTPL	6,020,402	5,793,790
Derivative assets – mandatorily measured at FVTPL	(47,829)	(18,235)
	5,972,573	**5,775,555**

Foreign investments include K4.3 billion (2019: K4.1billion) of investments managed by external fund managers. The remainder of K1.7 billion (2019: K1.7 billion) is managed directly by the Bank. The investments comprise of foreign bank debt securities, sovereign debt securities and over-the-counter derivative currency contracts.

Note 10: GOVERNMENT OF PAPUA NEW GUINEA SECURITIES

	2020 K'000	2019 K'000
Inscribed stock – measured at FVTPL	1,478,939	2,113,222
Treasury bills – measured at Amortised Cost	180,202	295,748
	1,659,141	**2,408,970**

Note 11: LOANS AND ADVANCES

	2020 K'000	2019 K'000
Agricultural export commodity support loans	1,386	1,386
Loans and advances to staff (including housing loans)	5,120	3,940
Temporary advances facility to PNG government	-	125,481
Allowance for doubtful loans	(4,714)	(4,714)
	1,792	**126,093**

The Temporary Advance Facility is governed by the provisions of the *Central Banking Act 2000*. The interest rate charged is the 6 monthly Treasury bills rate, approximately 7.2% p.a. The facility limit has increased from K200 million to K1.5 billion in 2020. As at 31 December 2020 there was no TAF overdraft balance.

The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained based on the Bank's credit evaluation of the counterparty. Collateral may include:

- A floating charge over all assets and undertaking of an entity;
- Specific or inter-locking guarantees;
- Specific charge over defined assets of the counterpart and
- Loan agreements including affirmative and negative covenants.

The loans and advances are measured at amortised cost. The related expected credit loss allowances are immaterial. Accordingly, detailed disclosure regarding expected credit loss impairment has not been made.

Note 12: OTHER ASSETS

	2020 K'000	2019 K'000
Inventory notes and coins	22,188	27,354
Commemorative notes & coins and other receivables	(337)	(298)
Prepaid employee benefits	40,509	35,333
Other non-financial assets	10,370	6,318
	72,730	**68,707**

Note 13: PROPERTY AND EQUIPMENT

	Land and Buildings at Fair Value K'000	Equipment K'000	Motor Vehicles K'000	Computer Equipment K'000	Computer Software K'000	ROU Asset K'000	Capital Work-In-Progress K'000	Total K'000
At 31 December 2019								
Cost or fair value	288,375	38,397	5,801	16,725	42,758	16,855	82,705	491,616
Accumulated depreciation	-	(9,366)	(2,705)	(10,574)	(16,179)	(4,368)	-	(43,192)
Net Book Amount	**288,375**	**29,031**	**3,096**	**6,151**	**26,579**	**12,487**	**82,705**	**448,424**
Year ended 31 December 2020								
Opening net book amount	288,375	29,031	3,096	6,151	26,579	12,487	82,705	448,424
Additions	3,238	2,537	757	914	-	1,430	20,698	29,574
Reclass/Transfers	-	-	-	-	-	-	-	-
Revaluation	-	-	-	-	-	-	-	-
Disposals	-	-	(23)	-	-	-	-	(23)
Depreciation charges	(14,705)	(1,665)	(1,205)	(1,544)	(4,080)	(4,279)	-	(27,478)
Closing Book Amount	**276,908**	**29,903**	**2,625**	**5,521**	**22,499**	**9,638**	**103,403**	**450,497**
At 31 December 2020								
Cost or fair value	276,908	40,934	5,843	17,639	42,758	18,285	103,403	505,770
Accumulated depreciation	-	(11,031)	(3,218)	(12,118)	(20,259)	(8,647)	-	(55,273)
Net Book Amount	**276,908**	**29,903**	**2,625**	**5,521**	**22,499**	**9,638**	**103,403**	**450,497**

The Bank's increase in Property and equipment during the year pertains primarily to capital work-in-progress additions.

Land and buildings carried at fair value

The fair values of land and building carried at fair value were determined by external, independent property valuers, having appropriate recognised professional qualifications and recent experience in location and category being valued. The independent valuers provide the fair value of the Bank's properties on a triennial basis. The most recent valuation was done in 2019. A desktop valuation was performed in 2020.

The carrying amount of land and buildings had they been recognised under the cost model are Land K8.5 million (2019: K8.5 million) and Buildings K230 million (2019: K227 million).

	2020 K'000	2019 K'000
Note 14: INVESTMENT PROPERTIES		
Balance at 1 January	39,170	41,460
Acquisitions	-	-
Reclassification from property and equipment	-	-
Change in fair value	-	(2,290)
Balance at 31 December	**39,170**	**39,170**

Investment property comprises two commercial properties that are leased to third parties. The fair values of investment properties were determined by external, independent property valuers, having appropriate recognised professional qualifications and recent experience in location and category being valued. The independent valuers provide the fair value of the Bank's investment property every 3 years. The most recent valuation was done in 2019. A desktop valuation was performed in 2020. The fair value measurements for all of the investment properties have been categorised as level 3 fair value measurements. Rental income from investment properties is K5.1 million (2019: K4.7 million).

Note 15: DEPOSITS FROM BANKS & THIRD PARTIES

	2020 K'000	2019 K'000
Banks		
Exchange settlement accounts	2,037,176	1,525,278
Cash reserve requirement	1,570,868	2,089,930
Other Deposits	11,094	10,629
	3,619,138	**3,625,837**

Note 16: DEPOSITS FROM GOVERNMENT AND GOVERNMENT ENTITIES

	2020 K'000	2019 K'000
Deposits from Government and Government entities	1,623,971	1,351,160
	1,623,971	**1,351,160**

Note 17: DEBT SECURITIES ISSUED

	2020 K'000	2019 K'000
Central Bank Bills issued	1,612,924	1,775,731
	1,612,924	**1,775,731**

Securities issued are debt securities issued by the Bank of Papua New Guinea for terms of twenty-eight days, three or four months. CBB Bond has tenures 1 – 10 years. These bills are used to manage liquidity in the money supply and open market operations in the domestic financial markets.

Note 18: CURRENCY IN CIRCULATION

	2020 K'000	2019 K'000
Currency in circulation	2,431,093	2,298,574
	2,431,093	**2,298,574**

Currency in circulation represents currency issued having a claim on the Bank of Papua New Guinea. The liability for currency in circulation is recorded at face value, which is equivalent to its fair value in the Statement of Financial Position.

	2020 K'000	2019 K'000
Note 19: OTHER FINANCIAL LIABILITIES		
Foreign currency		
Foreign currency deposits	5,697	1,794
	5,697	**1,794**
Local currency		
Expense creditors	52,700	38,871
Lease liability	10,177	12,860
	62,877	**51,731**

Expense creditors include cheques or warrants issued by the Bank but not yet presented for clearance and subsequent encashment by Government departments, investors and suppliers.

	2020 K'000	2019 K'000
Note 20: PROVISIONS FOR EMPLOYEE ENTITLEMENTS		
Provision for gratuity	5,896	4,497
Provision for long service leave	24,630	22,532
Provision for annual leave	5,438	6,769
	35,964	**33,798**
Reconciliation of leave provisions		
Balance at 1 January	33,798	27,961
Net charged to Statement of Profit or Loss	2,166	5,837
Balance at 31 December	**35,964**	**33,798**

Note 21: LEASES

A. Leases as lessee

Right-of-use assets

Right-of-use assets relate to leased offices and warehouses that are presented within property and equipment.

	2020 K'000	2019 K'000
Balance at 1 January	12,487	15,200
Depreciation charge for the year	(4,279)	(4,368)
Additions	1,430	1,655
Balance at 31 December	**9,638**	**12,487**

Lease liabilities

The following table sets out a maturity analysis of lease payments, included under Other financial liabilities on Note 24(iii)(c).

	2020 K'000	2019 K'000
One to three months	1,063	1,074
Three to twelve months	3,266	2,756
One to five years	5,848	9,030
	10,177	**12,860**

	2020 K'000	2019 K'000
Amounts recognised in Profit or Loss		
2019 – Leases under IFRS 16		
Interest expense on lease liabilities	683	882
Expenses relating to short-term leases	4,112	4,799
Amounts recognised in statement of cash flows		
Total cash outflow for leases	9,073	10,050

B. Leases as lessor

Operating lease

The Bank leases out its investment property. The Bank has classified these leases as operating leases, because they do not transfer substantially all of the risks and rewards incidental to the ownership of the assets.

The following table sets out a maturity analysis of lease receivables, showing the undiscounted lease payments to be received after the reporting date.

	2020 K'000	2019 K'000
2020 – Operating leases under IFRS 16		
Less than one year	3,876	3,635
One to two years	225	386
Two to five years	-	32
More than five years	-	-
Total	**4,101**	**4,053**

Note 22: SHARE CAPITAL

At 31 December 2020, the authorised and subscribed capital of the Bank was K145.5 million (2019: K145.5 million). The capital is fully subscribed by the Government of Papua New Guinea.

	2020 K'000	2019 K'000
Capital		
At the beginning of the year	145,540	145,540
At the end of the year	**145,540**	**145,540**
Other Reserves		
Gold revaluation reserve	258,995	197,412
Property revaluation reserve	95,028	95,028
Unrealised gain/(loss) reserve	573,890	299,888
Building reserve	123,800	73,800
General reserve	30,000	30,000
Retained earnings	378,457	418,662
Total other reserves	**1,460,170**	**1,114,790**
Total owner's equity	**1,605,710**	**1,260,330**

Note 23: SEGMENT REPORTING

The Bank's primary function as a central bank is the implementation of monetary policy in one geographical area - Papua New Guinea.

Note 24: RISK MANAGEMENT

Note 24(i): Financial Risk Management

International Financial Reporting Standard (IFRS) 7 – Financial Instruments: Disclosures – requires disclosure of information relating to financial instruments, their significance, performance, accounting policy, terms and conditions, fair values and the Bank's policies for controlling risks and exposures relating to the financial instruments.

A financial Instrument is defined as any contract that gives rise to both a financial asset of one enterprise and financial liability or equity instrument of another entity. The identifiable financial instruments for Bank of Papua New Guinea are its domestic Government securities, its foreign government securities, loans and advances, bank deposits, Central Bank Bills, currency in circulation and deposit liabilities.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Bank of Papua New Guinea's recognised instruments are carried at amortised cost or current market value.

The Bank is involved in policy-oriented activities. Therefore, the Bank's risk management framework differs from the risk management framework for most other financial institutions. The main financial risks to which the Bank is exposed include commodity price risk, credit risk, foreign exchange risk, liquidity risk and interest rate risk. In the management of foreign reserves, minimising liquidity risk is the prime consideration in order to ensure the availability of currency as required. Like most central banks, the nature of the Bank's operations creates exposure to a range of operational and reputational risks.

Bank management seeks to ensure that strong and effective risk management and control systems are in place for assessing, monitoring and managing risk exposure. Experienced staffs conduct the Bank's local currency, foreign currency reserves management, and foreign exchange dealing operations in accordance with a clearly defined risk management framework, including delegated authority limits as set by the Governor.

The Bank is subject to an annual audit by an external auditor. Auditing arrangements are overseen by an Audit & Governance Committee of the Board to monitor the financial reporting and audit functions within the Bank and the Committee reviews the internal audit functions as well. The Committee reports to the Board of Directors on its activities.

The overall risk management framework is designed to strongly encourage the sound and prudent management of the Bank's risk. The Bank seeks to ensure the risk management framework is consistent with financial market best practice. The risks tables in this note are based on the Bank's portfolio as reported in its Statement of Financial Position.

Note 24(ii): CREDIT RISK

(a) Credit risk management

Credit risk is the potential for financial loss arising from a counterparty defaulting on its obligation to repay principal, make interest payments due on an asset, or settle a transaction.

The Bank manages credit risk by employing the following strategies:

- Selection of a counterparty is made based on their respective credit rating. Investment decisions are based on the credit rating of the particular issuer, the issue size, country limits and counterparty limits in place to control exposures.
- Foreign currency placements are made in approved currencies with Government, Government guaranteed or other approved counterparties. Geographical exposures are controlled by country limits. Limits are updated periodically where necessary based on the latest market information. Credit risk in the Bank's portfolio is monitored, reviewed and analysed regularly.

(b) Concentration of credit exposure

The Bank's end-of-year concentrations of credit exposure by industry type were as follows:

	2020 K'000	2019 K'000
Foreign governments, banks & financial organisations		
Nostro accounts	3,074,377	1,804,862
Foreign investments (note 9)	5,972,573	5,775,555
Assets held with IMF and other financial organisations	30,510	30,209
Accrued interest receivable	19,024	19,714
Papua New Guinea Government		
Government of Papua New Guinea securities (Note 10)	1,659,141	2,408,970
Temporary advance to PNG Government (Note 11)	-	125,481
Accrued interest receivable TAF	5,236	-
PNG commercial banks (Note 11)	-	-
Bank staff and employees (Note 11)	5,120	3,940
Other Government Institutions (Note 11)	1,386	1,386
	10,767,367	**10,170,117**

The Bank's maximum exposure to credit risk is limited to the amount of financial assets carried in the Statement of Financial Position. 6% (2019: 22%) of the total assets have a credit rating of A-1+ or above in short term investments and 49% (2019: 34%) of long term investments have a credit of A+ or above.

(c) Credit exposure by credit rating

The following table represents the Bank's financial assets based on Standard and Poor's and Moody's credit ratings of the issuer. Under Standard and Poor's ratings, AAA is the highest quality rating possible and indicated the entity has an extremely strong capacity to pay interest and principal, AA is a high grade rating, indicating a very strong capacity, and A is an upper medium grade, indicating a strong capacity; BBB is the lowest investment grade rating, indicating a medium capacity to pay interest and principal. Non-rated ('NR') indicates the entity has not been rated by Standard and Poor's and Moody's.

Investment in Financial Assets	2020 K'000	% of 2020 Financial Assets	2019 K'000	% of 2019 Financial Assets
Short term foreign investments				
A-1+	431,994	6	1,783,152	22
A-1	443,971	6	147,583	1
A-2	-	-	69,244	1
A-3	-	-	-	-
NR	(39,703)	-	148,056	2
	836,262	**12**	**2,148,035**	**26**
Long term foreign investments				
AAA	1,307,560	17	2,157,719	26
AA+	-	-	-	-
AA	2,463,094	32	631,787	8
AA-	-	-	-	-
A+	-	-	-	-
A	793,876	10	426,528	5
A-	-	-	-	-
BBB+	-	-	-	-
BBB	548,365	8	411,486	5
BBB-	23,416	-	-	-
	5,136,311	**67**	**3,627,520**	**44**
Total foreign investments	**5,972,573**	**79**	**5,775,555**	**70**
Short term domestic investments				
B-	180,202	2	295,748	4
	180,202	**2**	**295,748**	**4**
Long term domestic investments				
B-	1,478,939	19	2,113,222	26
	1,478,939	**19**	**2,113,222**	**26**
Total domestic investments	**1,659,141**	**21**	**2,408,970**	**30**
Total investments	**7,631,416**	**100**	**8,184,525**	**100**

The majority of financial assets are measured at FVTPL. The ECL allowances related to the Treasury bills, loans and advances measured at amortised cost and loans to the PNG Government, are immaterial, hence no quantitative disclosure of ECL have been made. No financial assets designated at FVTPL have been reclassified to amortised cost.

Note 24(iii): Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate and currency products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads and foreign exchange rates.

(a) Foreign exchange risk

Currency risk (foreign exchange rate risk) is a form of risk that arises from the change in price of one currency against another, which directly affects the value of foreign exchange reserves as well as investments. At the Bank, foreign exchange reserve management and investment functions are guided by an Investment Committee. The decision of the Investment Committee and dealing practices approved by the Investment Committee serve as operational guidelines for the Bank's reserve management and investments. The guidelines are directed towards managing different types of risks, while earning a reasonable return. There is an approved benchmark for investment in terms of currency composition, portfolio duration and proportion of different assets within the Bank. Dealers/portfolio managers endeavour to comply with this benchmark through rebalancing the investment portfolio following benchmarking daily/weekly as approved by the Investment Committee. The currency of denomination of gold assets is USD.

As at 31 December 2020 Bank of Papua New Guinea's net exposure to major currencies in kina terms was as follows:

	CURRENCY OF DENOMINATION							
As at 31 December 2020	USD K'000	Euro K'000	AUD K'000	GBP K'000	JPY K'000	SDR K'000	Other K'000	Total K'000
Foreign Currency Assets:								
Foreign currency	1,877,941	76,653	926,581	140,096	49,813	-	3,293	3,074,377
Investments	4,913,563	132,734	935,934	38,171	-	-	-	6,020,402
Derivative assets	(47,829)	-	-	-	-	-	-	(47,829)
Assets held with IMF	-	-	-	-	-	30,510	-	30,510
Accrued interest	16,354	854	1,794	22	-	-	-	19,024
	6,760,029	**210,241**	**1,864,309**	**178,289**	**49,813**	**30,510**	**3,293**	**9,096,484**
Foreign Currency Liabilities:								
Liabilities with IMF	-	-	-	-	-	640,069	-	640,069
Foreign currency liabilities	5,697	-	-	-	-	-	-	5,697
	5,697	**-**	**-**	**-**	**-**	**640,069**	**-**	**645,766**
Net Foreign Currency exposure	**6,754,332**	**210,241**	**1,864,309**	**178,289**	**49,813**	**(609,559)**	**3,293**	**8,450,718**

As at 31 December 2019	CURRENCY OF DENOMINATION							
	USD K'000	Euro K'000	AUD K'000	GBP K'000	JPY K'000	SDR K'000	Other K'000	Total K'000
Foreign Currency Assets:								
Foreign currency	1,041,914	70,865	597,198	65,014	20,434	-	9,437	1,804,862
Investments	4,719,841	84,087	897,411	92,451	-	-	-	5,793,790
Derivative assets	(18,235)	-	-	-	-	-	-	(18,235)
Assets held with IMF	-	-	-	-	-	30,209	-	30,209
Accrued interest	17,763	220	1,677	54	-	-	-	19,714
	5,761,283	**155,172**	**1,496,286**	**157,519**	**20,434**	**30,209**	**9,437**	**7,630,340**
Foreign Currency Liabilities:								
Liabilities with IMF	-	-	-	-	-	597,335	-	597,335
Foreign currency liabilities	1,794	-	-	-	-	-	-	1,794
	1,794	**-**	**-**	**-**	**-**	**597,335**	**-**	**599,129**
Net Foreign Currency exposure	**5,759,489**	**155,172**	**1,496,286**	**157,519**	**20,434**	**(567,126)**	**9,437**	**7,031,211**

The functional currency of all operations is kina.

(b) Interest rate risk

Interest rate risk is the risk that the fair value or cash flows of financial instruments will fluctuate because of movements in market interest rates. The Bank is exposed to considerable interest rate risk because most of its assets are financial assets, such as domestic and foreign securities, which have a fixed income stream. The price of such securities increases when market interest rates decline, while the price of a security due to the associated income stream is fixed for a longer period.

The Bank manages interest rate risk by investing in securities with different maturity dates to mitigate against any adverse fluctuation in interest rates.

(c) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities in its operations. The ultimate source of liquidity is kina and the Bank has the authority to create liquidity by issuing unlimited amounts of kina.

Liquidity risk is also associated with financial assets to the extent that the Bank may have to sell a financial asset at less than its fair value. The Bank manages this risk by holding a diversified portfolio of highly liquid domestic and foreign assets. The Bank's assets held for managing liquidity risk comprise cash and bank balances with other central banks and Government bonds and other securities that are readily acceptable in repurchase agreements with other central banks.

The table below summarises the maturity profile of the Bank's financial liabilities based on the contractual repayment date determined on the basis of the remaining period at the reporting date to the contractual maturity date.

As at 31 December 2020	Balance Total K'000	MATURITY PROFILE On demand K'000	0 to 3 months K'000	3 to 12 months K'000	1 to 5 years K'000	Over 5 years K'000	No specified maturity K'000
Assets							
Foreign Currency Financial Assets:							
Cash and cash equivalents	3,074,377	2,730,410	343,967	-	-	-	-
Financial assets at fair value	5,972,573	-	958,053	973,255	3,471,925	569,340	-
Assets held with IMF	30,510	-	-	-	-	-	30,510
Accrued interest	19,024	-	1,737	5,044	11,691	552	-
	9,096,484	**2,730,410**	**1,303,757**	**978,299**	**3,483,616**	**569,892**	**30,510**
Local Currency Financial Assets:							
Government of Papua New Guinea Securities	1,659,141	-	122,758	334,747	729,125	472,511	-
Loans and advances	1,792	-	1,792	-	-	-	-
Accrued interest and receivables	38,663	-	7,072	31,591	-	-	-
	1,699,596	**-**	**131,622**	**366,338**	**729,125**	**472,511**	**-**
Non-Financial Assets:							
Gold	279,602	-	-	-	-	-	279,602
Property and equipment	450,497	-	-	-	-	-	450,497
Investment properties	39,170	-	-	-	-	-	39,170
Other financial assets	72,730	-	-	-	-	-	72,730
	841,999	**-**	**-**	**-**	**-**	**-**	**841,999**
Total Assets	**11,638,079**	**2,730,410**	**1,435,379**	**1,344,637**	**4,212,741**	**1,042,403**	**872,509**
Liabilities							
Foreign Currency Financial Liabilities:							
Liabilities with IMF	640,069	-	-	-	-	-	640,069
Other financial liabilities	5,697	-	5,697	-	-	-	-
	645,766	**-**	**5,697**	**-**	**-**	**-**	**640,069**
Local Currency Financial Liabilities:							
Deposits from banks and third parties	3,619,138	3,619,138	-	-	-	-	-
Deposits from Government	1,623,971	1,623,971	-	-	-	-	-
Securities issued	1,612,924	-	765,687	29,373	65,774	752,090	-
Accrued interest payable	636	-	636	-	-	-	-
Currency in circulation	2,431,093	2,431,093	-	-	-	-	-
Lease liability	10,177	-	1,063	3,266	5,848	-	-
Other financial liabilities	52,700	-	52,700	-	-	-	-
	9,350,639	**7,674,202**	**820,086**	**32,639**	**71,622**	**752,090**	**-**
Non-Financial Liabilities:							
Employee Provision	35,964	-	35,964	-	-	-	-
Total Liabilities	**10,032,369**	**7,674,202**	**861,747**	**32,639**	**71,622**	**752,090**	**640,069**

As at 31 December 2019	Balance Total K'000	MATURITY PROFILE On demand K'000	0 to 3 months K'000	3 to 12 months K'000	1 to 5 years K'000	Over 5 years K'000	No specified maturity K'000
Assets							
Foreign Currency Financial Assets:							
Cash and cash equivalents	1,804,862	915,250	889,612	-	-	-	-
Financial assets at fair value	5,775,555	-	1,461,471	671,788	3,264,278	378,018	-
Assets held with IMF	30,209	-	-	-	-	-	30,209
Accrued interest	19,714	-	16,451	724	2,539	-	-
	7,630,340	**915,250**	**2,367,534**	**672,512**	**3,266,817**	**378,018**	**30,209**
Local Currency Financial Assets:							
Government of Papua New Guinea securities	2,408,970	-	-	295,747	375,800	1,737,423	-
Loans and advances	126,093	-	126,093	-	-	-	-
Accrued interest and receivables	58,947	-	517	10,493	10,441	37,496	-
	2,594,010	**-**	**126,610**	**306,240**	**386,241**	**1,774,919**	**-**
Non-Financial Assets:							
Gold	218,020	-	-	-	-	-	218,020
Property and equipment	448,424	-	-	-	-	-	448,424
Investment properties	39,170	-	-	-	-	-	39,170
Other financial assets	68,707	-	-	-	-	-	68,707
	774,321	**-**	**-**	**-**	**-**	**-**	**774,321**
Total Assets	**10,998,671**	**915,250**	**2,494,144**	**978,752**	**3,653,058**	**2,152,937**	**804,530**
Liabilities							
Foreign Currency Financial Liabilities:							
Liabilities with IMF	597,335	-	-	-	-	-	597,335
Other financial liabilities	1,794	-	1,794	-	-	-	-
	599,129	**-**	**1,794**	**-**	**-**	**-**	**597,335**
Local Currency Financial Liabilities:							
Deposits from banks and third parties	3,625,837	3,625,837	-	-	-	-	-
Deposits from Government	1,351,160	1,351,160	-	-	-	-	-
Securities issued	1,775,731	-	1,297,426	31,001	67,270	380,034	-
Accrued interest payable	2,381	-	2,381	-	-	-	-
Currency in circulation	2,298,574	2,298,574	-	-	-	-	-
Lease liability	12,860	-	1,074	2,756	9,030	-	-
Other financial liabilities	38,871	-	27,242	-	-	11,629	-
	9,105,414	**7,275,571**	**1,328,123**	**33,757**	**76,300**	**391,663**	**-**
Non-Financial Liabilities:							
Employee provision	**33,798**	**-**	**33,798**	**-**	**-**	**-**	**-**
Total Liabilities	**9,738,341**	**7,275,571**	**1,363,715**	**33,757**	**76,300**	**391,663**	**597,335**

Note 24(iv): Fair value

"Fair value" is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the bank has access at that date. The fair value of a liability reflects its non-performance risk. IFRS requires that the fair value of the financial assets and liabilities be disclosed according to their classification under IFRS 9. The following table summarises the financial assets and liabilities in accordance with IFRS 9 classifications.

	2020 K'000	2019 K'000
Financial Assets		
Cash and cash equivalents	3,074,377	1,804,862
At fair value through profit/(loss)	7,482,022	7,918,987
Loans & advances measured at amortised cost	59,479	204,754
Treasury bills measured at amortised cost	180,202	295,747
	10,796,080	**10,224,350**
Financial Liabilities		
At fair value through profit/(loss)	645,766	599,129
At amortised cost	9,350,639	9,105,414
	9,996,405	**9,704,543**

Fair values are estimated to be the same as their carrying values in the Statement of Financial Position.

Fair value hierarchy

IFRS 13 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchanges.
- Level 2 – inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes over-the-counter derivative contracts. The sources of input parameters are Bloomberg or Reuters.
- Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components.

The table below shows the Bank's assets and liabilities in their applicable fair value level. Investments managed by external fund managers include foreign government bonds and other debt instruments for which quoted prices are available, as well as derivatives which are valued with reference to observable market data. Accordingly, these are classified under level 1 and 2 respectively.

	Level 1 K'000	Level 2 K'000	Level 3 K'000	Total K'000
31 December 2020				
Financial assets held at fair value through profit or loss				
Domestic Government securities - Inscribed stock	-	-	1,478,939	1,478,939
Foreign Government and semi-government bonds	1,661,499	-	-	1,661,499
Derivatives managed by external fund managers	-	(47,829)	-	(47,829)
Investments in bonds and other instruments managed by external fund managers	4,358,903	-	-	4,358,903
Assets held with IMF	-	30,510	-	30,510
Total assets at fair value through profit or loss	**6,020,402**	**(17,319)**	**1,478,939**	**7,482,022**
Non-financial assets at fair value				
Gold	279,602	-	-	279,602
Property and equipment	-	-	450,497	450,497
Investment property	-	-	39,170	39,170
Total assets at fair value	**279,602**	**-**	**489,667**	**769,269**
Financial liabilities held at fair value through profit & loss				
Derivatives	-	5,697	-	5,697
Liabilities with IMF	-	640,069	-	640,069
Total liabilities at fair value through profit or loss		**645,766**	**-**	**645,766**
31 December 2019				
Financial assets held at fair value through profit or loss				
Domestic Government securities - Inscribed stock	-	-	2,113,223	2,113,223
Foreign government and semi-government bonds	1,709,398	-	-	1,709,398
Derivatives managed by external fund managers	-	(18,235)	-	(18,235)
Investments in bonds and other instruments managed by external fund managers	4,084,392	-	-	4,084,392
Assets held with IMF	-	30,209	-	30,209
Total assets at fair value through profit or loss	**5,793,790**	**11,974**	**2,113,222**	**7,918,987**
Non-financial assets at fair value				
Gold	218,020	-	-	218,020
Property and equipment	-	-	448,424	448,424
Investment property	-	-	39,170	39,170
Total assets at fair value	**218,020**	**-**	**487,594**	**705,614**
Financial liabilities held at fair value through profit & loss				
Derivatives	-	1,794	-	1,794
Liabilities with IMF	-	597,335	-	597,335
Total liabilities at fair value through profit or loss	**-**	**599,129**	**-**	**599,129**

As at 31 December 2020, there were no movements between stages for any transfers to level 3.

The following table presents the changes in Level 3 financial instruments (excluding the accrued interest) for year ended 31 December 2020:

	Level 3 K'000
Opening balance	**2,113,222**
Maturities/disposals, net of additional investment	(591,920)
Fair value revaluation gains/(losses) on level 3 instruments	(42,363)
Closing balance	**1,478,939**
Total gains and (losses) for the period included in the Profit or Loss for level 3 assets held at the end of the reporting period.	**(42,363)**

The following table presents the changes in Level 3 financial instruments (excluding the accrued interest) for year ended 31 December 2019:

	Level 3 K'000
Opening balance	2,067.450
Maturities/disposals, net of additional investment	(39,298)
Fair value revaluation gains/(losses) on level 3 instruments	85,070
Closing balance	**2,113,222**
Total gains and losses for the period included in the Profit or Loss for Level 3 assets held at the end of the reporting period.	**85,070**

	Valuation Technique	Unobservable Input	Range of Inputs		Fair value movement due to change in unobservable Input	
			2020	2019	Increase	Decrease
Domestic Government securities – Inscribed stock and Treasury bills	Discounted cash flows present value method	Current market yield	8% to 12.5%	8% to 14%	Decrease	Increase
Investment property	Income capitalisation	Capitalisation rate	10% to 14%	10% to 14%	Stable	Increase

Note 24(v): Sensitivity analysis

The sensitivity of the Bank's profit and equity to a movement of +/- 10 percent in the value of the kina as at 31 December 2020 is shown below. These figures are generally reflective of the Bank's exposure over the fiscal year.

	2020 K'000	2019 K'000
Changes in profit/equity due to a 10 percent appreciation in the value of the kina	(937,609)	(784,836)
Changes in profit/equity due to a 10 percent depreciation in the value of the kina	937,609	784,836

The figures below show the effect on the Bank's profit and equity of a movement of +/- 1 percentage point in interest rates, given the level, composition and modified duration of the Bank's interest bearing assets and liabilities.

	2020 K'000	2019 K'000
Changes in profit/equity due to an increase of 1 percentage point	93,506	90,925
Changes in profit/equity due to a decrease of 1 percentage point	(93,506)	(90,925)

Note 25: EVENTS AFTER THE BALANCE DATE

At the date of finalisation of the annual financial statements, there were no material events that occurred subsequent to the Statement of Financial Position date that require adjustment to the financial statements.

Note 26: CONTINGENT LIABILITIES

The Bank had no contingent liabilities at 31 December 2020 (2019: nil) and there are no transactions or events that will have material impact on the financial report during the preparation of this report.

The Bank is a party to a number of litigations, the outcome of which are currently uncertain. The directors, Governor and the Deputy Governor in consultation with the Bank's legal advisors consider that these litigations are not expected to result in material loss to the Bank.

Note 27: CAPITAL COMMITMENTS

The Bank has no capital commitments.

Note 28: REMUNERATION OF MEMBERS OF THE BOARD AND KEY MANAGEMENT PERSONNEL

IAS 24 – Related party disclosures requires disclosure of information relating to aggregate compensation of key management personnel. The key management personnel of the Bank are members of the Board and senior staff who have responsibility for planning, directing and controlling the activities of the Bank. This group comprises 29 in total (2019: 32), including the Governor, 1 Deputy Governor, 4 Assistant Governors, 4 non-executive Board members and 20 senior staff. The Salaries and Remuneration Committee (SRC) and Salaries, Conditions & Monitoring Committee (SCMC) determine the terms and conditions on which the Governor and Deputy Governor hold office in accordance with the *Central Banking Act 2000*. The Governor, in consultation with the Salaries, Conditions & Monitoring Committee (SCMC), determines the remuneration of other key executives.

Key Management Personnel Remuneration

	2020 K'000	2019 K'000
Short term benefits	16,202	12,078
Post-employment benefits	1,008	907
Other long term benefits	7,542	6,753
	24,752	**19,738**

Short term benefits include cash salary and in the case of staff, annual leave and motor vehicle, housing benefits and superannuation which can be accessed prior to retirement. Post-employment benefits include superannuation benefit payments which can be accessed on retirement. Other long term benefits include long service leave and benefits related to loans and advances to staff. The components of benefits are reported on an accruals basis.

As at 31 December 2020 the loans owed by the key management personnel to the Bank were K6,019,475 (2019: K4,300,192).

Note 29: AUDITOR'S REMUNERATION

The total audit fee for the year was K1,352,656 (2019: K1,340,625). This represents the total statutory audit fee paid to the Auditor General's Office and other auditors in relation to external fund manager operations. These transactions are performed at arm's length.

Note 30: TRANSACTIONS WITH GOVERNMENT AND GOVERNMENT CONTROLLED ENTERPRISES

The Bank of Papua New Guinea acts as the banker to the Government and its various Government departments and controlled enterprises. The Government of Papua New Guinea is restricted under the *Central Banking Act 2000* in actively participating in Bank's decision and policy formulations. All related party transactions are carried out with reference to market rates. Transactions entered into include:

(a) Acting as the fiscal agent, banker and financial advisor to the Government, the Bank is the depository of the Government and or its agents or institutions providing banking services to Government and Government departments and corporations.

(b) Acting as the agent of the Government or its agencies and institutions, providing guarantees, participating in loans to Government departments and corporations.

(c) As the agent of the Government managing public debt and foreign reserves.

Balances with the Government of Papua New Guinea are disclosed in note 16 Deposits from Government and Government Entities and note 11 for TAF reflecting Government loan balances with BPNG.

Transactions with the Government of Papua New Guinea are disclosed in Note 3 Interest revenue – domestic operations.

Declaration by Management

DECLARATION BY MANAGEMENT

In our opinion the foregoing Statement of Profit or Loss and other Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity and Statement of Cash Flows including the Notes to and forming part thereof, have been drawn up so as to give a true and fair view of the matters to which they relate for the year ended 31 December 2020.

For and on behalf of the Bank of Papua New Guinea,

Loi Martin Bakani CMG
Governor

Joseph Michael Teria
Deputy Governor

30 June 2021

Report of the Auditor-General

AUDITOR-GENERAL'S OFFICE
PAPUA NEW GUINEA

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Our Reference: 30-13-4

The Honourable Ian Ling-Stuckey, MP
Minister for Treasury
Office of the Minister
PO Box 542
WAIGANI, NCD

INDEPENDENT AUDIT REPORT
ON THE ACCOUNTS OF
BANK OF PAPUA NEW GUINEA
FOR THE YEAR ENDED 31 DECEMBER 2020

OPINION

I have audited the financial statements of **Bank of Papua New Guinea,** which comprise the Statement of Financial Position as at **31 December 2020**, Statement of Profit or Loss and Other Comprehensive Income, Statement of Changes in Equity, Statement of Cash Flows and Summary of Significant Accounting Policies and Other Explanatory Notes;

In my opinion:

(a) the financial statements of Bank of Papua New Guinea for the year ended 31 December 2020:

(i) give a true and fair view of the financial position and of its financial performance and cash flows for the year then ended; and

(ii) comply with the *International Financial Reporting Standards*, *Papua New Guinea Central Banking Act 2000* and other generally accepted accounting practice in Papua New Guinea; and

(b) proper accounting records have been kept by the Bank as far as it appears from my examination of those records; and

(c) I have obtained all the information and explanation that were required.

BASIS FOR OPINION

I conducted my audit in accordance with *International Standards on Auditing* and the *Audit Act, 1989 (as amended)*. My responsibilities under those standards are further described in the Auditor-General's responsibilities for the audit of the financial statements section of my report.

I am independent of the Bank of Papua New Guina in accordance with the ethical requirements that are relevant to my audit of the financial statements in Papua New Guinea, and I have fulfilled my other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Responsibilities of the Board, the Governor and the Deputy Governor of the Bank for the Financial Statements

The Bank's Management is responsible for the preparation and fair presentation of the financial statements in accordance with the *International Financial Reporting Standards* and *Papua New Guinea Central Banking Act 2000* and for such internal control as the Management determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, Management is also responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the Independent State of Papua New Guinea either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

The Management is responsible for overseeing the Bank's financial reporting process.

Auditor-General's Responsibilities for the Audit of the Financial Statements

My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with *International Standards on Auditing* will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial statements.

As part of an audit in accordance with the *International Standards on Auditing*, I exercise professional judgement and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control;

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management;

- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions may cast significant doubt on the Bank's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my audit report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my report. However, future events or conditions may cause the Bank to cease to continue as a going concern; and

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

I communicate with the Management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

GORDON KEGA MBA, CPA
Auditor-General

27 October, 2021

Notes


BANK OF PAPUA NEW GUINEA